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In the Supreme Court of the United States

OCTOBER TERM, 1971

No. 71–

UNITED STATES OF AMERICA, PETITIONER

v.

UNITED STATES STEEL CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

OPINIONS BELOW

The opinion of the district court on the "raw materials" Korean War excess profits tax relief issue, with respect to which review is sought here (Appendix A, *infra*, pp. 15–33), is reported at 305 F. Supp. 497, and its opinion on reargument (Appendix B, *infra*, pp. 35–47) is reported at 305 F. Supp. 516. The opinion of the court of appeals, reversing the district court (Appendix C, *infra* pp. 49–85), is reported at 445 F. 2d 520.

JURISDICTION

The judgment of the court of appeals was entered on June 22, 1971 (Appendix D, *infra*, pp. 87–88). By order dated September 22, 1971, Mr. Justice Harlan extended the time for filing a petition for a writ of certiorari to and including November 19, 1971. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

The Korean War excess profits tax law (Section 442(a) (1) and (2) of the Internal Revenue Code of 1939) provides relief from the tax if a taxpayer establishes that, for any taxable year within its base period, "normal production, output, or operation" was interrupted or diminished by "events unusual and peculiar in the experience of such taxpayer," or if the business of the taxpayer was depressed by reason of "temporary economic circumstances unusual in the case of such taxpayer * * *."

The question presented is whether respondent could qualify for relief under either of these provisions, if it could establish that its steel production or profits during its base period years 1947 and 1948 had been reduced as a result of the effects of World War II—the exhaustion of high grade iron ore and coal ("raw materials") earlier than it had anticipated, and shortages of men and materials which delayed the implementation of steps to offset the low quality of raw materials that it was forced to utilize.

STATUTE INVOLVED

Internal Revenue Code of 1939 (26 U.S.C. (1952 ed.)):

SEC. 442 [as amended by Sec. 509 of the Revenue Act of 1951, c. 521, 65 Stat. 452, 549–550]. AVERAGE BASE PERIOD NET INCOME—ABNORMALITIES DURING BASE PERIOD.

(a) IN GENERAL.—If a taxpayer which commenced business on or before the first day of its base period establishes that, for any taxable year within, or beginning or ending within, its base period:

(1) normal production, output, or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during such taxable year, of events unusual and peculiar in the experience of such taxpayer, or

(2) the business of the taxpayer was depressed because of temporary economic circumstances unusual in the case of such taxpayer,

the taxpayer's average base period net income determined under this section shall be the amount computed under subsection (c) or (d), whichever is applicable.

* * * * *

STATEMENT

Respondent instituted this action in the district court [1] seeking refund of some $27.77 million paid as

[1] The jurisdiction of the district court rested on 28 U.S.C. 1346(a).

income and Korean War excess profits taxes and interest for the year 1950, on the grounds that it had been erroneously denied an additional deduction for depletion and upon various claims for excess profits tax relief (Appendix C, *infra*, pp. 50, 66–67; R. 21a–25a, 695a–710a).[2] The district court decided all of the questions in the government's favor except one of the relief issues,[3] and its decision resulted in a judgment for respondent of approximately $974,000 (R. 19a), from which the government did not appeal (Appendix C, *infra*, p. 67). On respondent's appeal, the court of appeals affirmed in all respects (Appendix C, *infra*, pp. 50–85) except as to another of the relief issues—respondent's claim that it was entitled to relief under Section 442 with respect to its base period years 1947 and 1948 by reason of the poor quality of its "raw materials," iron ore and coal. The district court had decided that issue for the government on a summary judgment motion, but the court of appeals reversed and remanded for trial (Appendix C, *infra*, pp. 74–85).

For present purposes, the facts with respect to the "raw materials" relief issue, which were assumed by the court of appeals to be true (Appendix C, *infra*, p. 74), may be summarized as follows:

Respondent, a manufacturer and seller of iron and steel products, for years before World War II, utilized mainly high grade iron ore and coal from its

[2] "R." references are to the two-volume joint appendix filed in the court of appeals, a copy of which we have lodged with the Clerk of this Court.

[3] See the final opinion of the district court, disposing of the entire case after trial on the remaining issues (R. 621a–710a), which is reported at 316 F. Supp. 990.

own mines as its principal raw materials in making steel. As a result of the large World War II demand for steel, respondent exhausted its high grade iron ore and coal more quickly than had been anticipated, and utilized lower grade ores and coal, with a correspondingly higher content of impurities. This, in turn, required resort to increased beneficiating facilities (such as washers, etc.). During the period 1947–1948, respondent was unable to establish adequate beneficiating facilities by reason of such factors as war-induced shortages of men and materials, and delays by suppliers and subcontractors. In consequence, it suffered losses in steel production tonnage and in profits for the years 1947 and 1948. (Appendix C, *infra*, pp. 74–78; R. 208a, 210a–211a, 226a–227.)

Based upon these assumed facts, respondent contended that it qualified for relief from the Korean War excess profits tax in the form of an increased credit. In general, the excess profits tax (Sections 430 *et seq.* of the 1939 Code), applicable to the years 1950 through 1953, consisted of an additional tax on all corporate profits in excess of a certain level or norm, called the "excess profits credit," deemed to represent a taxpayer's "normal" profits. That credit was to be computed either on the basis of the taxpayer's average earnings during a specified prior period (called the "base period;" generally the years 1946–1949) or on the basis of invested capital, whichever resulted in the lesser tax—except that the law contained several provisions granting "relief" for hardship cases or dealing with special situations.

Section 442 of the 1939 Code (p. 3, *supra*), under which respondent sought to qualify, in subsection (a)(1), authorizes relief if a taxpayer establishes that, for any taxable year within (or beginning or ending within) its base period, "normal production, output or operation" was interrupted or diminished by the occurrence of "events unusual and peculiar in the experience of such taxpayer"; subsection (a)(2) authorizes relief if the business of the taxpayer was depressed by reason of "temporary economic circumstances unusual in the case of such taxpayer." If a taxpayer qualifies for relief under either of these provisions, the law provides for the use of an excess profits credit arrived at (instead of on the basis of a reconstruction of the taxpayer's own base period earnings) by the automatic application of a mathematical formula, *i.e.*, by applying to the amount of the taxpayer's total base period assets, as of the end of its base period years, the base period rate of return for the taxpayer's industry classification as prescribed by the Commissioner of Internal Revenue pursuant to Section 447. If Section 442(a) applies to two or more years during the base period, then Section 442(d) provides that the constructive income resulting from use of the appropriate industry rate (if it exceeds 110 percent of actual income) is to be used for all three years of the base period, after elimination of the most unfavorable of the four base period years, as permitted by Section 435(d)(2). The relief provision, if applicable, thus has the effect of increasing the excess profits credit, and thereby decreasing or eliminating the excess profits subject to the special tax.

In granting the government's motion for summary judgment on the so-called "raw materials" relief issue, the district court held that the combined effects of World War II which caused reduced production and profits in 1947 and 1948—the earlier than anticipated exhaustion of high grade raw materials, resulting in the use of lower grade materials during these years, coupled with shortages of men and materials, and delays by suppliers and subcontractors which prevented the establishment of adequate beneficiating facilities—could not, as a matter of law, qualify as "unusual and peculiar" events or as unusual "temporary economic circumstances" within the meaning of Section 442(a) (1) or (2) (Appendix A, *infra*, pp. 23–33; Appendix B, *infra*, pp. 46–46). The court of appeals reversed (Appendix C, *infra*, pp. 74–85).

REASONS FOR GRANTING THE WRIT

1. The court of appeals has interpreted the statute in a manner inconsistent with the purpose reflected in the structure of the relief provisions as they evolved in the Korean War excess profits tax law, and with the congressional intent underlying the grant of relief.

The Korean War law, though substantially derived from the World War II excess profits tax law (Section 710, *et seq*, of the 1939 Code), had changes reflecting experience under the earlier law, especially in the approach to the grant of special relief, and particularly in those categories which had been covered in the "general relief" provisions of the World War II law (Section 722). The latter pro-

visions had caused considerable difficulty, both because of the requirement of the reconstruction of a hypothetical, "tailor-made" constructive average base period net income for each qualifying taxpayer, and because of the many subjective or discretionary factors entering into the determination of qualification for relief. The Korean War relief provisions (Sections 442–446) granted relief on separate and distinct grounds, each with its own qualification tests, and its own specific conditions, all expressly and separately enumerated for each category of relief authorized. Once entitlement to relief was established, the measure of relief was prescribed through mathematical formulae.

The net result of the changes was that the various situations with respect to which relief had been provided under the prior law were, after being in most instances narrowed or restricted, included within automatic provisions or eliminated, thereby avoiding the necessity for "subjective judgments" in determining qualification for, and the measure of, relief. See H. Rep. No. 3142, 81st Cong., 2d Sess., pp. 15–24; S. Rep. No. 2679, 81st Cong., 2d Sess., pp. 17–28; see also, *Jarecki* v. *G. D. Searle & Co.*, 367 U.S. 303. In short, Congress chose in the Korean War law to limit relief to a few specifically and carefully delineated grounds, rather than to grant a theoretically more perfect pattern of relief that would take into account the innumerable factors that might adversely affect a taxpayer's business and operations during the base period. As Senator George, Chairman of the Senate Finance

Committee, explained (96 Cong. Rec., Part 12, p. 16770), Congress' view was that it is "better to provide a less perfect adjustment quickly under a prescribed formula than to strive for a more refined result" and risk the pitfalls of old Section 722.

Section 442(a)(1), which requires the occurrence of "events unusual and peculiar in the experience" of the taxpayer, was intended to afford relief primarily for a physical interruption to production, such as a "fire, strike or flood." Section 442(a)(2), which requires "temporary economic circumstances unusual" in the case of the taxpayer, was aimed at purely "economic circumstances such as a severe price war." See H. Rep. No. 3142, 81st Cong., 2d Sess., p. 17; S. Rep. No. 2679, 81st Cong., 2d Sess., pp. 18–19; Treasury Regulations 130 (excess profits tax), Sec. 40.442–1, 2 (as amended by T.D. 5973, 1953–1 Cum. Bull. 321). Unless Section 442(a)(1) is read expansively, it is difficult to see how the effects of World War II on respondent—its sooner than anticipated exhaustion of high grade raw materials, and shortages of men and materials which delayed the establishment of adequate beneficiating facilities—can properly be considered "events" occurring within the base period within the meaning of the statute. As for the question whether such exhaustion and shortages constitute "temporary economic circumstances unusual" in the case of the taxpayer under Section 442(a)(2), our position is that the term "temporary" should not be interpreted to include a combination of circumstances that develop and persist over a period of years, and that "unusual" should be read, consistently with

Congress' purpose to confine relief to specific situations, so as not to extend relief to the many taxpayers which were in some way adversely affected by World War II.

Since World War II undoubtedly had some adverse effects on the post-war operations of most corporations, the implication of the holding below is that all taxpayers would be eligible for relief if they could prove the causal connection between World War II and depressed base period earnings. The holding below also implies that the courts are to consider the almost endless variety of the complex and indirect effects of World War II in applying Section 442(a). Unlike the typical "event" such as a "fire, strike, or flood," or typical "temporary economic circumstances" such as a "severe price war," all of which have only unfavorable results, World War II inevitably brought to every taxpayer both benefits and detriments.[4] Thus, this kind of detailed analysis introduces "the very type of subjective judgments" that Congress sought to avoid by its introduction of the "automatic" provisions with respect to qualification for (as well as the amount of) relief. H. Rep. No. 3142, 81st Cong., 2d Sess., p. 20; S. Rep. No. 2679, 81st Cong., 2d Sess., p. 24.

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[4] Although respondent alleges that the "war-induced shortages of men and materials, particularly engineers and draftsmen, steel, steel fabricated products, [and] electrical equipment" prevented "normal development and expansion of beneficiating facilities" (R. 211a), it has admitted that the demand for steel during these years was "unprecedented" (R. 341a).

Finally, it seems clear that Congress could not have intended to grant relief to respondent on the generalized theory that its 1947–1948 production was diminished or its business depressed during those years. As the court of appeals itself recognized (Appendix C, *infra*, p. 78, n. 26, pp. 81–82), 1947 and 1948 were two of the best years in respondent's history in terms of both production and earnings. With regard to production, 1947 was exceeded only by 1941, 1942 and 1944, and 1948 was exceeded only by 1944. Respondent's after-tax earnings in 1947 and 1948 were the highest since 1929. Congress was aware, when it enacted the Korean War excess profits tax law, of respondent's profitability during 1947 and 1948. The legislative history discloses that respondent was named as one of the corporations at which the excess profits tax was directed, and that the high profits which respondent and other named, large corporations enjoyed in 1947 and 1948 were regarded by Congress, in part, as justification for the tax. See 96 Cong. Rec., Part 12, pp. 16093, 16149. Despite this, the court of appeals has held that "*something* may have been going wrong at U.S. Steel during the base period" (Appendix C, *infra*, p. 82), as a result of the effects of World War II, which prevented respondent's production and profits from being even greater. In so holding, the court has opened the way for respondent to reduce its excess profits tax liability for the total Korean War period by 80 percent, through use of the general relief or hardship provision.

2. The magnitude of the reduction in excess profits tax liability is such as to make this tax case one of the largest involving a single taxpayer in the history of the internal revenue laws. An aggregate of $230 million of taxes and interest turns upon the raw materials relief issue.[5] The specific holding of the court of appeals—that the effects of World War II may qualify a taxpayer for Korean War excess profits tax relief—is unprecedented. Practically every taxpayer subject to the excess profits tax must have felt some impact of World War II on its base period operations in some manner. Yet, in more than two decades of judicial and administrative construction of the Korean War law, the notion that the effects of World War II could be sifted out and made a ground for relief had not appeared prior to the opinion of the court of appeals in this case.

The consequence of this novel construction of the statute at this late date is that respondent (and per-

[5] For the year in suit, 1950, respondent will be entitled to an additional refund of more than $25 million, plus interest, on the raw materials relief issue, if it is successful in establishing the facts at trial (R. 37a). But apart from the year in suit, respondent's income and excess profits tax liability for 1951–1953 is still pending administratively on claims similar to those for 1950. If successful on remand of the instant case, respondent will by res judicata become entitled to additional excess profits tax relief for those years under the computation formula of Section 442 (d). The Internal Revenue Service advises that the excess profits tax liability of respondent for all of the years subject to the Korean War excess profits tax (1950 through 1953), turning on the raw materials relief issue, amounts to more than $107 million of tax, plus interest, which brings the total to approximately $230 million.

haps one other corporation [6]) will have the opportunity to obtain excess profits tax relief on a theory unavailable to all other taxpayers similarly situated. They are already barred from obtaining relief by the statute of limitations.

Under these special circumstances, the decision below cannot be dismissed as lacking in administrative importance on the usual ground that the outcome of the litigation turns upon the construction of a provision of the internal revenue laws which is no longer in effect. Administrative significance is not to be evaluated alone in terms of a suitable vehicle for the declaration by this Court of a particular technical rule for the disposition or avoidance of future controversies. The fiscal impact of this case is itself important. Moreover, any tax case that could weaken public confidence in the fairness of the federal taxing system is, to that extent, administratively important. If the opportunity to obtain excess profits tax relief on the theory accepted below is to be granted to one or two large corporations—and to no others—it should be granted only after full review by this Court.

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[6] In *Citadel Industries, Inc.*, v. *United States*, now pending in the United States District Court for the Southern District of New York (70 Civ. 385), the total refund claimed is more than $7 million, plus statutory interest. One of the issues in that case is whether the taxpayer may qualify for relief under Section 442 because, among other things, restrictions imposed upon it by the War Production Board hindered its development of a successful diesel locomotive.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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NOVEMBER 1971.

APPENDIX A

Opinion of Judge Levet Dated July 1, 1969

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

Opinion Motion No. 2 [1]

LEVET, D. J.

The United States of America, the above-entitled defendant, has moved under Rule 56 of the Federal Rules of Civil Procedure for summary judgment with respect to the claim of the plaintiff for refund of 1950 excess profits tax payments set forth in paragraphs 9, 10, 11 and 12 of the complaint, dealing with the low quality of coking coal and iron ore.

The relevant claims alleged in the complaint are as follows:

"Denial of Application of §442

> "9. Plaintiff duly filed with its consolidated Federal income and excess profits tax return for 1950 a claim that, in determining its excess profits credit, its consolidated 'average base period net income' should be determined in accordance with § 442 of the Internal Revenue Code of 1939.
>
> "10. In determining the Federal income tax for 1950 which Plaintiff has paid, Plaintiff's aforesaid claim for the application of § 442 has been denied.

[1] The defendant's first motion for summary judgment, denying plaintiff's claim for depletion deductions, was granted May 19, 1967, 270 F. Supp. 253 (S.D.N.Y. 1967).

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"11. For 1950, Plaintiff's consolidated 'average base period net income' should have been calculated by reference to § 442, because, within the meaning of § 442(a), during the base period years 1947 and 1948, Plaintiff's normal production was diminished by reason of the occurence during that period of events unusual and peculiar in the experience of the Plaintiff, and Plaintiff's business was depressed because of temporary economic circumstances unusual in the case of the Plaintiff. Such temporary abnormality was low quality of coking coal and iron ore, resulting in loss of production.

"12. Plaintiff's consolidated 'average base period net income' for 1950 should be computed in accordance with §442."

The complaint is an action under Section 1346(a)(1) of Title 28 United States Code to recover federal income tax for the year 1950 and assessed interest on additional payments of such tax, which plaintiff claims were erroneously and illegally assessed and collected.

Relevant Statute

The relevant statute from the Internal Revenue Code of 1939 is as follows:

"§442. *Average base period net income—abnormalities during base period*

"(a) *In general.* If a taxpayer which commenced business on or before the first day of its base period establishes that, for any taxable year within, or beginning or ending within, its base period:

"(1) normal production, output, or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during such taxable year, of *events unusual and peculiar in the experience of such taxpayer*, or [emphasis added]

"(2) the business of the taxpayer was depressed because of *temporary economic circumstances unusual in the case of such taxpayer,* [emphasis added] the taxpayer's average base period net income [shall be] * * * determined under this section * * *."

Claim of the United States

The United States contends that the occurrences put forth by the United States Steel Corporation as abnormalities during the base period years of 1947 and 1948 do not qualify as "events unusual and peculiar" or as "temporary economic circumstances unusual" in the case of such taxpayer within the meaning of 26 U.S.C. Excess Profits Taxes, § 442(a)(1) or (a)(2). More specifically, the defendant's contention is as follows: Plaintiff has failed to establish that the shortages of men and materials which delayed development of beneficiating facilities for coking coal and iron ore during 1947 and 1948, and the shortages of steel scrap and coal available for purchase by plaintiff during said years, consisted of more than (1) occurrences affecting business in general; and (2) reasonably-expected competitive pressures.

The Contention of the Plaintiff

The plaintiff, on the other hand, contends that the occurrences cited qualify as abnormalities justifying general relief within the meaning of the statute.

Issue

The issue before the court on this motion for summary judgment involves the excess profits tax provided for by the Internal Revenue Code of 1939 and may be stated as follows:

"Do the war-induced shortages of men and materials which delayed plaintiff's development of beneficiating facilities for coking coal and iron ore during 1947 and 1948, and the shortages of steel scrap and coal available for purchase during said years, constitutes 'events unusual and peculiar' or 'temporary economic circumstances unusual' in the case of such taxpayer within the meaning of 26 U.S.C. Excess Profits Taxes. § 442(a)(1) or (a)(2)?"

Facts

The following facts are derived from the Joint Rule 9(g) Statement submitted by the parties May 1, 1969:

1. In general, plaintiff has continually developed facilities for removing impurities from iron ore and coking coal as mined. Such beneficiating facilities are employed to the extent necessary to render these two important materials suitable for charging into blast furnaces as part of the overall steel-making process. (§§ 28, 29, Joint Rule 9(g) Statement)

2. During the period 1941 to 1948, plaintiff was unable to maintain normal development and expansion of said facilities because of war-induced shortages of men and materials, particularly engineers and draftsmen, steel, steel fabricated products, electrical equipment and delays by suppliers and subcontractors. (§ 16)

3. During 1947 and 1948, the iron ore and coking coal charged to plaintiff's blast furnaces contained more impurities than in any other relevant year.[2] (§§ 14, 15)

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[2] For the purposes of this motion, the parties have stipulated that 1941, 1942, 1943, 1944, 1950, 1951 and 1953 are the relevant years outside the base period. See exhibits attached to Joint Rule 9(g) Statement.

4. During 1947 and 1948, plaintiff's normal production was diminished and its business was depressed due to the high degree of impurities, as mentioned above. The presence of so great a quantity of impurities was the result of the delay in development of beneficiating facilities during 1947 and 1948 because of war-induced shortages of men and materials. (§ 62)

5. The coal available for purchase by plaintiff from independent producers during 1947 and 1948 was less suitable for use in iron and steel production than the coal obtainable in prior or subsequent years. The shortage of acceptable quality coal obtainable by plaintiff during said years was caused by an abnormally high demand coupled with a relatively short supply. The low quality of the coal purchased by plaintiff from independent producers during 1947 and 1948 contributed in part to the low quality of the totality of coal charged to plaintiff's coking ovens and blast furnaces during said years, although the extent of the purchased coal's influence on the low quality of the totality of coal charged cannot be measured from existing records. (§§ 57, 84, 114)

6. The steel scrap available for purchase by plaintiff during 1947 and 1948 was less suitable for use in steel production than the steel scrap obtainable in prior years. (§§ 10, 20)

The plaintiff paid to the District Director of Lower Manhattan, New York City, additional federal income taxes for 1950 with interest. The time for assessment against plaintiff of additional federal income tax for 1950 was extended to June 30, 1966. Plaintiff filed a claim on June 29, 1965 for refund of federal income tax paid for 1950 and interest thereon, in such amount as may be legally refundable, with interest.

The claim was rejected on August 24, 1965. (Plaintiff's complaint, paragraphs 4–7; defendant's answer, admissions relating to said paragraphs.) The claim for general relief from the excess profits tax payments for 1950 because of low quality coking coal and iron ore constituted part of the claim filed June 29, 1965.

THE PROPERTY OF SUMMARY JUDGMENT

It is elementary that summary judgment may be rendered when there is no genuine issue as to any material fact and the movant is entitled to judgment as a matter of law. Rule 56, F.R. Civ. P.

When a motion for summary judgment is made and supported, the adverse party must set forth specific facts or evidentiary data showing that there is a genuine issue for trial. Rule 56(e), F.R. Civ. P.; Dressler v. M/V Sandpiper, 331 F. 2d 130, 133 (2nd Cir. 1964); Scolnick v. Lefkowitz, 329 F. 2d 716, 717 (2nd Cir. 1964), cert. denied, 379 U.S. 825 (1964).

Plaintiff submitted a statement alleging material facts as to which it contended there are genuine issues to be tried. (Plaintiff's statement appended to Joint Rule 9(g) Statement, pp. 20–23). In response, defendant submitted a statement declaring that each of the material facts set forth by plaintiff had already been admitted by defendant as part of the Joint Rule 9(g) Statement. (Defendant's letter to the court, May 2, 1969).

Plaintiff asserts that summary judgment on the present motion would be inappropriate for four reasons, each of which, it develops, is insufficient to preclude the entry of such judgment.

First, plaintiff alleges that there exists a disputed material fact as to whether there was any direct correlation between the increased use of mechanical load-

ing devices at plaintiff's coal mines during 1947 and 1948 and the increased content of impurities in the coking coal during said years. (Plaintiff's statement, p. 20).

Second, plaintiff alleges that whether it had any practical or realistic alternative to the increased use of such devices constitutes a material fact in genuine dispute. (Plaintiff's statement, p. 20)

Defendant, in a subsequent response, stated that for the purposes of this motion it was withdrawing its earlier arguments on the use and impact of mechanical loading devices at plaintiff's mines. (Defendant's letter to the court,[3] May 2, 1969, p. 4, referring to defendant's memorandum of law, March 28, 1969, pp. 78–80)[4]

Plaintiff continues to maintain that disputed material facts remain as to these issues. (Stenographer's minutes of hearing, June 3, 1969, p. 82) However, in light of defendant's abandonment of its earlier arguments regarding mechanical loading devices, I find that neither of the plaintiff's allegations mentioned above presents a material fact genuinely in dispute.

Third, plaintiff alleges that its "evidence at trial may adduce additional events and economic circumstances which diminished its production and depressed its business in 1947 and 1948." (Plaintiff's statement, p. 22)

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[3] On April 25, 1969, the court requested the parties to prepare a Joint Rule 9(g) Statement and submit supplementary letters, as a further means of clarifying their positions. The Joint 9(g) Statement was submitted May 1, 1969, and plaintiff's and defendant's letters were transmitted to the court on May 1 and May 2, 1969, respectively.

[4] Originally, defendant argued (1) that plaintiff increased use of mechanical loading devices during the period from 1941 to 1948; (2) that increased use of the devices contributed to

It is well established, however, that a party opposing a motion for summary judgment is not entitled to rely on the hope of a subsequent magical appearance at trial of genuine issues of material fact. See Fitzgerald v. Westland Marine Corporation, 369 F. 2d 499, 500 (2nd Cir. 1966); Engl v. Aetna Life Ins. Co., 139 F. 2d 469, 472–473 (2nd Cir. 1943); Erickson v. Said, 42 F.R.D. 170, 173 (S.D.N.Y. 1967); Kaz Manufacturing Co. v. Chesebrough-Pond's, Inc., 211 F. Supp. 815, 819–820 (S.D.N.Y. 1962), aff'd, 317 F. 2d 679 (2nd Cir. 1963).

Fourth, plaintiff alleges that the occurrences giving rise to its claim cannot be understood fully in the absence of testimony from "live witnesses" at trial. (Plaintiff's statement, pp. 22–23) Where motive, intent and credibility are material issues of fact, particularly in complex antitrust litigation, testimony of live witnesses may be desirable and summary judgment may therefore be inappropriate. See White Motor Co. v. United States, 372 U.S. 253, 259 (1963); Poller v. Columbia Broadcasting System, 368 U.S. 464, 472–473 (1962); see also American Manufacturers Mutual Insurance Co. v. American Broadcasting-Paramount Theatres, Inc., 388 F. 2d 272, 279–280 (2nd Cir. 1967).

In the instant case, plaintiff has put forth no specific facts to indicate that any of these factors is relevant to or has any impact upon the material issues for the purposes of this motion, which involve the existence of *external* factors affecting plaintiff's business dur-

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the low quality of coking coal during 1947 and 1948; and (3) that, in effect, loss of production or depression in business for plaintiff was due to an internal management decision to increase use of the devices, rather than to an external causative factor, which would be required in order to qualify for relief under § 442.

ing 1947 and 1948. The parties agree that certain factors were indeed existent. (See Facts, above) Furthermore, plaintiff has made no suggestion that any material fact has been unavailable to date by reason of being within the movant's exclusive knowledge or control. See 6 Moore's Federal Practice § 56.24, at 2876 (2nd ed. 1966).

Accordingly, I conclude that there is no genuine issue as to any material fact.

The Law

I

Background of the Statute

The Excess Profits Tax Act of 1950, 26 U.S.C. Excess Profits Taxes, §§ 430 et seq., which is designed to tax at high rates unusually high profits earned during the Korean War, imposes a tax on profits in excess of an amount deemed to represent the taxpayer's normal profits. Jarecki v. G. D. Searle & Co., 367 U.S. 303, 304 (1961).

The object of relief provisions under both the Korean War Act and its predecessor, the World War II Excess Profits Tax Act of 1940, 26 U.S.C. Excess Profits Taxes, §§ 710 et seq., is to ensure that the finally derived average base period net income should reflect what the taxpayer would have earned in the excess profits tax year (i.e., 1950) but for the war which may have fortuitously increased profits.

In furtherance of this objective, actual base period net income which is unrepresentative for a statutorily-defined reason should be replaced by a constructive income. Oxford Paper Company v. Commissioner, 302 F. 2d 674, 681 (2nd Cir. 1962).

Since Sections 442(a)(1) and (a)(2) are essentially identical to Sections 722(b)(1) and (b)(2), their

counterparts under the World War II Act, judicial interpretation of the earlier provisions may be utilized to ascertain the meaning of the Korean Act provisions. 7A Mertens, Law of Federal Income Taxation (Zimet & Weiss rev. 1955) § 42.109, at p. 545; see Oxford Paper Company v. Commissioner, supra; Fulton Foundry & Machine Co., 26 T.C. 953, 956 (1956), aff'd per curiam 249 F. 2d 445 (6th Cir. 1957).

II

Burden of Proof

In order to warrant general relief under the statute, the taxpayer has the burden of establishing a qualifying abnormality which caused its business to be depressed during the relevant base period years of 1947 and 1948.

The Tax Court, in disallowing a petitioner's claim for relief in Alexandria Amusement Corp., 16 T.C. 446, 455 (1951), stated that:

> "* * * [S]ection 722 is not a means of extending equitable aid to all taxpayers affected by the excess profits tax: Section 722 affords relief, not on broad equitable principles, but only if certain conditions existed. * * *"

The above statement is as appropriate to the present case as it was to prior cases decided under Section 722, the forerunner of Section 442.

Establishment of a specific external qualifying factor is a prerequisite to relief.

III

Exercise of Governmental Power

The valid exercise of governmental power does not constitute the basis for relief under either Section

442(a)(1) or (a)(2). Seekonk Lace Co., 24 T.C. 552, 563 (1955); United Motor Coach Co., 22 T.C. 578, 580–581 (1954); see also Del Mar Turf Club, 16 T.C. 749, 763–764 (1951); Alexandria Amusement Corp., supra, at 456; Acme Breweries, 14 T.C. 1034, 1052 (1950).

Accordingly, World War II itself does not qualify either as an unusual and peculiar event or as an unusual temporary economic circumstance within the meaning of the statute. Plaintiff has acknowledged the inappropriateness of the war as a qualifying factor. (See plaintiff's reply memorandum of law, May 21, 1969, pp. 6, 7)

Plaintiff argues that reactions to valid governmental activity may constitute unusual and peculiar events or unusual temporary economic circumstances affording relief. Assuming, arguendo, that such reactions are not automatically barred as abnormalities entitling a taxpayer to relief under the statute, it is, nevertheless, undeniable that specific external qualifying factors must be established by a plaintiff who petitions for such relief.

IV

The Issue Under Section 442(a)(1)—Unusual And Peculiar Events

The intended scope of the statutory term "event" is clearly indicated by Reg. 130 (1939 Code) § 40.442–2 (a)(3):

> "* * * Unusual and peculiar events contemplated in section 442(a)(1) consist primarily of physical rather than economic events or circumstances. Such physical events include floods, fires, explosions, strikes, and other exceptional and uncommon circumstances hindering production, output, or operation."

Cases under both Sections 722(b)(1) and 442(a)(1) further demonstrate what types of events are contemplated under both the World War II and Korean provisions. Among such cases are New York Shipbuilding Corp. v. Commissioner, 362 F. 2d 550, 551 (3rd Cir. 1966) (strike); Oxford Paper Co. v. Commissioner, 302 F. 2d 674, 677 (2nd Cir. 1962) (drought); Burford-Toothaker Tractor Co. v. United States, 262 F. 2d 891, 892 (5th Cir. 1959) (strike against major supplier); Schneider's Modern Bakery, Inc., 19 T.C. 763, 772 (1953) (strike); Avey Drilling Machine Co., 16 T.C. 1281, 1292 (1951) (flood); see also 7A Mertens, supra, § 42.119, n. 55 at p. 703, quoting Bulletin on Section 722 of the Internal Revenue Code (November, 1944), pp. 10–11 (severe freeze or blizzard, a crop blight or epidemic, or a temporary court injunction).

Plaintiff relies on the following illustration which was deemed a qualifying abnormality in the Bulletin on Section 722, supra, at p. 18, quoted in 7A Mertens, supra, § 42.121, n. 42 at p. 726:

> "A brush manufacturing company which normally imports most of its bristles from China suffered an impairment of its business and earnings during the base period *because of the Japanese invasion of China in 1937*. It had to seek elsewhere for its raw material and accept inferior substitutes at higher prices. This interruption of raw material supplies constitutes a temporary economic event affecting the taxpayer and its industry which would be recognized [as a qualifying abnormality]." (Emphasis added)

The situation outlined above is readily distinguishable from the case at hand. The Japanese invasion which occurred during the base period for the World

War II statute was a qualifying event. The ensuing shortage which resulted in a depression of the hypothetical taxpayer's business was an effect directly attributable to the invasion itself.

In the instant matter, plaintiff has suggested shortages as abnormalities, without any reference to a further factor as a possible cause of the shortages. It should be noted that the Mertens text describes the qualifying abnormality set forth in the Bulletin as an "interruption in supplies caused by war." 7A Mertens, supra, § 42.121, at p. 726.

Plaintiff has set forth no physical event of the type contemplated by the statute, regulations or case law interpretation. I conclude, therefore, that the war-induced shortages of men and material which delayed development of beneficiating facilities for coking coal and iron ore during 1947 and 1948, and the shortages of steel scrap and coal available for purchase by plaintiff during said years do not constitute qualifying *events* within the meaning of the statute.

Plaintiff has failed to establish that it is entitled to relief under § 442(a)(1).

V

The Issue Under Section 442(a)(2)—Unusual Temporary Economic Circumstances

(A) *War-induced Shortages of Men and Materials which Delayed Development of Beneficiating Facilities During 1947 and 1948.*

Plaintiff, attempting to establish a qualifying abnormality under Section 442(a)(2), again cites war-induced shortages of men and materials which delayed development of beneficiating facilities during the relevant base period years of 1947 and 1948.

Plaintiff maintains (1) that said shortages were temporary economic circumstances which were unusual in the sense that they did not occur before or after; and (2) that circumstances are not barred from being considered unusual under the statute even though they may also have affected "a large number of people" in addition to the taxpayer. (SM, June 3, 1969, pp. 99, 100, 105).[5]

Defendant, on the other hand, contends that the war-induced shortages of men and materials were not unusual because "every single taxpayer in the period was subject to the same kinds of vicissitudes as that * * * (e)verybody wanted to shift from wartime production to peacetime demands." (SM, June 3, 1969, p. 108)

---

[5] Plaintiff has propounded war-induced shortages of men and materials during *1941 to 1948, inclusive*, as alleged abnormalities which delayed development of "washers" for coking coal and iron ore during *1947 and 1948*.

Shortages which occurred during *1941 to 1945* have been disregarded here as potential qualifying circumstances because they were inextricably intertwined with the United States government's exercise of its war powers during World War II. As previously discussed, the war itself is not a qualifying abnormality.

For the purposes of this motion, the court has considered primarily the post-war shortages occurring during the base period years of 1947 and 1948. It may be suggested that the 1941–1945 shortages, taken together with the 1947–1948 shortages, should be considered *in toto* as forming a pattern of shortages continuing throughout the war years and the post-war period of economic adjustment.

Thus, it may be argued that the 1947–1948 shortages would not qualify as *temporary* economic circumstances. See Dow Jones & Co., 41 T.C. 102, 128 (1963). However, it is unnecessary to decide this point in view of the court's disposition of the claim on other grounds; i.e., the shortages of men and materials during 1947 and 1948 were not unusual within the meaning of the statute.

In determining the intended scope of Section 442 (a)(2), it is helpful to consider the pertinent regulations for the Korean statute, as follows:

> "An event is unusual and peculiar in the experience of the taxpayer if its occurrence is not ordinarily encountered in the taxpayer's business operations. Such event may be unusual in the case of other taxpayers. For example, a flood in a particular locality may be unusual in the case of a number of taxpayers. * * * " Reg. 130 (1939 Code), § 40.422-2(a)(3).
>
> "As in the case of unusual and peculiar events interrupting or diminishing production, output, or operation, a temporary economic circumstance is unusual in the case of a taxpayer if its occurrence is not ordinarily encountered in that taxpayer's business operations. A temporary economic circumstance may be unusual in the case of a taxpayer even though it is also unusual in the case of other taxpayers. * * * " Reg. 130 (1939 Code), § 40.442-2(b)(2).

I interpret the regulations to mean that a taxpayer must establish specific circumstances which are unusual in two senses: (1) that they did not occur before or after the relevant base period years; and (2) that they affected only the immediate taxpayer and a reasonably-limited number of other taxpayers.

Absent such a twofold showing of unusualness, circumstances can only be ascribed to competitive pressures affecting business in general during the years involved.

Responding to questions by the court, plaintiff's counsel acknowledged that the record submitted for the purposes of this motion did not reveal (1) whether plaintiff had experienced prior manpower shortages, or (2) whether other steel producers experienced the same shortages during 1947 and 1948. (SM, June 3, 1969, pp. 101–102) When the court reminded him that

the taxpayer had the burden of establishing a qualifying abnormality in order to gain relief, plaintiff's counsel declared that in his opinion the Joint Rule 9(g) Statement and plaintiff's statement appended thereto were "clearly sufficient to bring us within [the statute]." (SM, June 3, 1969, pp. 102, 132) The court is unable to agree that plaintiff has made a showing sufficient to warrant relief.

First, there is no indication in the record on this motion that plaintiff has made any attempt to submit additional specific evidentiary data. Second, it is indisputable that plaintiff has had over twenty years since the shortages occurred to gather and submit any data which it may have determined would be helpful to its cause in the present case. Third, plaintiff presented no detailed statement at the hearing on this motion to contradict defendant's assertion that shortages of men and materials affected almost all businesses in the United States during 1947 and 1948. (See SM, June 3, 1969, pp. 107–135)

I find that the shortages of men and materials suggested by plaintiff do not qualify as unusual temporary economic circumstances within the meaning of Section 442(a)(2). Therefore, plaintiff has failed to sustain its burden with respect to that portion of its claim for relief dealing with said shortages during 1947 and 1948.

(B) *Shortages of Steel Scrap Obtainable by Plaintiff During 1947 and 1948.*

(C) *Shortages of Coal Obtainable by Plaintiff During 1947 and 1948.*

Plaintiff also contends that it is entitled to relief because of shortages of steel scrap and coal available for purchase during 1947 and 1948. Each of these contentions is insubstantial.

As to steel scrap, the amounts purchasable for charging to plaintiff's steel-making furnaces were lower in quality than in any *prior* relevant year, as measured by density and the percentage of contaminants contained in the scrap. Since plaintiff submits no evidence that the quality of the scrap obtainable improved significantly in *subsequent* years, I hold that plaintiff has failed to present a situation that may be characterized as temporary. (See § 10, Joint Rule 9(g) Statement)

As to coal, the amounts purchasable from independent producers for charging to plaintiff's coking ovens and blast furnaces were less suitable during 1947 and 1948 than in prior or subsequent years. The parties stipulate that the unavailability of acceptable quality coal was due to "abnormally high demand coupled with a relatively short supply," and that the low quality of the *coal available for purchase* contributed "in part" to the low quality of the *totality of coal* used by plaintiff during said years. The parties also agree that "the extent of the purchased coal's influence on [the strength of all coal charged to plaintiff's coking ovens and blast furnaces during 1947 and 1948] cannot be measured from existing records." (See §§ 57, 84, 114, Joint Rule 9(g) Statement)

Even if the low quality of purchasable coal did contribute to some unspecified extent to the low quality of the totality of coal used by plaintiff during 1947 and 1948, there is no indication in the record that the abnormally high demand and relatively short supply were caused by more than keen competitive pressures during these years. Such pressures must reasonably be expected by businessmen in the course

of their operations. See Interstate Milling Co., 32 T.C. 1038, 1047 (1959).

Plaintiff has not established that any steel scrap or coal shortages during 1947 and 1948 would justify relief under Section 442(a)(2).

Conclusion

The following principles defeat plaintiff's claims:

1. The burden is on the taxpayer to establish that its claims of abnormality during the base period years qualify for relief within the meaning of the statute.

2. The factors here consist of no more than (a) occurrences affecting business in general rather than plaintiff and a reasonably-limited number of other taxpayers, or (b) competitive pressures which businessmen must reasonably expect in the course of their operations. These factors do not qualify as "events unusual and peculiar" or "temporary economic circumstances unusual" in the case of such taxpayer under 26 U.S.C. Excess Profits Taxes, §442(a)(1) or (a)(2).

Consequently, defendant's motion for summary judgment is granted as to the claims in paragraphs 9, 10, 11 and 12 of the complaint relating to the low quality of coking coal and iron ore during 1947 and 1948. No genuine issue exists as to any material fact and the defendant is entitled to judgment as a matter of law.

For the reasons stated in my earlier memorandum dated July 14, 1967, unreported, I decline to insert a direction for entry of final judgment pursuant to Rule 54(b) of the Federal Rules of Civil Procedure. See also Gottesman v. General Motors Corporation, 401 F. 2d 510, 512 (2nd Cir. 1968); McNellis v.

Merchants National Bank and Trust Co. of Syracuse, 385 F. 2d 916, 919 (2nd Cir. 1967).

Settle judgment on notice.

RICHARD H. LEVET,
United States District Judge.

Dated: NEW YORK, N.Y., *July 1, 1969.*

APPENDIX B

Opinion and Order of Judge Levet Dated October 2, 1969

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

LEVET, D. J.

The plaintiff has moved for reargument of the court's decisions stated in opinions dated July 1, 1969.

I

Plaintiff maintains that the three basic conditions alleged in its complaint, namely (1) "low quality of coking coal and iron ore, resulting in loss of production;" (2) "abnormal cost-price relationships, resulting in the depression of Plaintiff's business and earnings;" and (3) "numerous and protracted strikes, resulting in the interruption and diminution of Plaintiff's normal production, output and operation;" (Complain, September 30, 1965, p. 3) "interact with one another so that, even if, contrary to plaintiff's firm insistence it should be concluded that no one claim in and of itself constituted, within the meaning of the statute, temporary economic circumstances unusual in the case of the taxpayer or events unusual and peculiar in the experience of the taxpayer, when all three claims are taken together there did occur such circumstances and events, and that plaintiff is entitled to aggregate those abnormalities to this end." (Plaintiff's memorandum, August 8, 1969, p. 8)

Apparently, the argument is as follows: Each of the three claims in and of itself should constitute a qualifying abnormality. However, even if the three claims do not qualify separately, the plaintiff should be entitled to aggregate them and submit them in combination so as to constitute one qualifying abnormality.

In support of this theory, plaintiff cites a paragraph from the Treasury Department Bulletin on Section 722 (November, 1944) which raises the possibility that "(a)n unusual combination or concurrence of usual conditions may of itself constitute an unusual event or condition under section 722(b)(2). For instance, a taxpayer's business may have been depressed during the base period because of an unusual combination of temporary economic circumstances, no one of which was unusual or would have abnormally depressed the business if existing alone." Treasury Department Bulletin on Section 722, Part III(B), cited in Standard Excess Profits Tax Reporter, volume 3A (1946), at ¶5145.12.

Plaintiff cites no decision where any court has either endorsed this general suggestion or discussed it; nor is this court aware of any. Indeed, the foreword to the Bulletin contains the comment that any provision therein "does not have the force or effect of a published ruling or of a Treasury decision. Id. at ¶5145.

Obviously, the Bulletin does not have the force of a judicial determination.

Even if a court did favor the general idea presented, it could not, in the absence of any guidelines, determine when a combination of separate non-qualifying conditions would constitute a qualifying abnormality and when such a combination would not. The Bulletin's hypothetical suggestion, therefore, not

only lacks any authoritative imprimatur (as indicated by the absence of even a scintilla of legislative or judicial support since the idea was advocated originally in 1944), but also lacks even a semblance of practicability.

II

Plaintiff maintains that the three conditions alleged in its complaint as qualifying abnormalities should not be adjudicated separately because they are "related by their application to plaintiffs production and the depression of plaintiff's business, and related by time and space." (Plaintiff's memorandum, September 22, 1969, p. 3)

However, separable issues (for purposes of interlocutory adjudication) may be presented in a tax refund action for a given year, even if only one "claims for relief" is said to be filed for each taxable year (for purposes of appealability under F.R.C.P. 54(b)).

It should be pointed out that final judgment in this case (in contrast to any interlocutory adjudication of separable issues which may constitute portions of a "claim for relief") must await judicial determination of all such issues. The parties agree that the third condition, propounded as a basis for relief under 442(a), involving "numerous and protracted strikes, resulting in the interruption and diminution of Plaintiff's normal production, output and operation," must be litigated at a forthcoming trial.

In determining whether separately adjudicable issues are present, a court analyzes the set of operative material facts specifically asserted as the underlying basis for each allegation of a qualifying abnormality. Each separate condition must stand on its

own as the first element required for relief is considered, i.e., whether a taxpayer has established a qualifying cause for any diminution of its production or depression of its earnings during the base period years. Establishment of one or more qualifying causes is a prerequisite to further consideration under 442 as to the amount of quantitative relief to which a taxpayer may be entitled for each year in question. If more than one qualifying cause is determined to exist, the effects of the separately-established causes may then be aggregated for quantitative considerations.

After the defendant had moved for summary judgment as to the issues in plaintiff's complaint dealing with "low quality of coking coal and iron ore, resulting in loss of production" (Motion #2) and "abnormal cost-price relationships, resulting in the depression of Plaintiff's business and earnings," (Motion #3) both parties submitted statements pursuant to General Rule 9(g) of the Southern District of New York.

In order to pinpoint the issues and "pierce the pleadings and * * * assess the proof in order to see whether there is a genuine need for trial," (Dressler v. MV Sandpiper, 331 F. 2d 130, 132 (2nd Cir. 1964)) the court requested the parties to prepare Joint 9(g) Statements delineating the facts which were not genuinely disputed for the purposes of the two motions, as well as separate statements setting forth any specific facts alleged to be in genuine dispute.

Subsequently, the parties submitted joint statements for Motion #2 (110 paragraphs) and Motion #3 (45 paragraphs). See the sections in the court's opinions on The Propriety of Summary Judgment.

The three basic conditions alleged as qualifying abnormalities are mentioned together in both joint state-

ments in identical paragraphs, which read in pertinent part as follows:

> "The occurrences depressing plaintiff's business and diminishing its production in 1947 and 1948 * * * included the imbalance between the inherent characteristics of constituent materials for blast furnace burdens as mined and the beneficiating facilities to adjust and transform such characteristics, strikes and an unusual labor relations situation, and an abnormally narrow cost-price gap, *each of which reacted on the other in contributing to the overall depression of plaintiff's business.*" (Emphasis added)
>
> Joint 9(g) Statement on Motion #2, ¶21;
> Joint 9(g) Statement on Motion #3, ¶19.

These paragraphs state that each of the three conditions contributed *quantitatively* to "the overall depression of plaintiff's business" during 1947 and 1948. However, the motions for summary judgment before the court dealt with the legal sufficiency on a *qualitative* basis of two of the three basic conditions put forth by plaintiff as qualifying abnormalities under § 442(a).

As discussed above, separate qualitative conditions may only be aggregated to determine their quantitative effect for each base period year after one or more of those separate conditions has been determined to constitute a qualifying abnormality.

It is one thing to say that each of the three basic conditions contributed quantitatively to a depression of plaintiff's business; it is quite another to say that each of the three conditions may not be considered separately in determining the existence of qualifying abnormalities.

The joint statement for Motion #2 contains no further reference to strikes. The joint statement for

Motion #3 refers to certain strikes as a prelude to wage settlements which increased plaintiff's costs. Insofar as wage settlements after strikes contributed to increased costs, such settlements are not a basis for relief under 442(a). See the court's opinion on Motion #3.

No material operative fact contained in either of the joint statements deals with plaintiff's third condition—strikes as a cause of diminished production. The notion that each of the conditions existed at some time during the base period years does not overcome the principle that separate conditions based on separate sets of operative facts may be adjudicated separately to determine the existence of a qualifying abnormality.

After studying the factual record before the court on both motions, I conclude that each of the three basic conditions alleged in paragraph 11 of plaintiff's complaint may be adjudicated separately.

III

Referring to Motion #2, plaintiff maintains that it should have further opportunity to come forward with some additional external cause for its delay in development of beneficiating facilities which is not directly attributable to World War II or to reasonably-expected competitive pressures. (Plaintiff's memorandum, September 3, 1969, pp. 2–5)

However, plaintiff admitted for purposes of Motion #2 that:

> "During the period 1941 to 1948, inclusive, because of such factors as war-induced shortages of men and materials, particularly engineers and draftsmen, steel, steel fabricated products, electrical equipment and delays by suppliers and subcontractors, plaintiff was unable to maintain normal development and ex-

pansion of beneficiating facilities." Joint 9(g) Statement for Motion #2, § 16.

As a matter of law, a taxpayer seeking relief under 442(a) must allege causative factors which are external to it, because the statute was not designed to counteract errors of business judgment or to underwrite unwise business policies. Granite Construction Co., 19 T.C. 163, 170 (1952).

Plaintiff had ample opportunity to submit any additional specific facts which it may have gathered by utilization of discovery techniques. However, plaintiff's only effort in this regard during the summary judgment proceedings was the submission of one affidavit in opposition to Motion #2. The affidavit, by Robert M. Lloyd, an employee of the plaintiff, refers to the delay in development of beneficiating facilities by stating that "(w)hat was unusual was the imbalance in available beneficiating facilities which had arisen earlier, the effect of which was experienced primarily in 1947 and 1948. This peculiar imbalance and abnormally poor furnace burden quality in 1947 and 1948 would never have occurred had it been possible for the Corporation to maintain and pursue its normal beneficiating program." (Affidavit in opposition to defendant's Motion #2, April 9, 1969, p. 10)

Plaintiff has suggested repeatedly, that "shortages of hot metal" or an "imbalance" between the quality of raw materials as mined and the beneficiating facilities available to render said raw materials suitable for steel-making were in and of themselves qualifying causes. However, the only specific external causative factors put forth for the delay in development of the facilities are contained in paragraph 16 of the Joint Statement for Motion #2.

As a matter of law, war-induced shortages of men and materials and delays by suppliers and subcontrac-

tors during the period of 1941 to 1948 may not constitute the basis for relief under 442(a), because effects directly attributable to United States government policies during World War II, including post-war competitive pressures engendered by wartime conditions, are not qualifying abnormalities within the meaning of the statute.

When a motion for summary judgment is made and supported by admissions on file, an adverse party may not rest upon the mere allegations or denials of his pleading, but his response must set forth specific facts showing there is a genuine issue for trial. If he does not so respond, summary judgment, if appropriate, shall be entered against him. Rule 56(e), F.R.C.P.; Waldron v. British Petroleum Co., 38 F.R.D. 170, 173–174 (S.D.N.Y. 1965), aff'd sub nom, Waldron v. Cities Service Co., 361 F. 2d 671, 672 (2nd Cir. 1966), aff'd sub nom, First National Bank of Arizona v. Cities Service Co., 391 U.S. 253, 289 (1968).

After the defendant had supported its motion with the admission contained in paragraph 16, plaintiff then had the burden of coming forward with specific facts to show the existence of a genuine issue for trial. Instead, plaintiff rested on its general allegations antedating the joint 9(g) statement. Plaintiff also suggested that additional causes for its delay in development of beneficiating facilities might be adduced at a trial, and that live witnesses would be necessary to explain the steel-making process. See the court's opinion on Motion #2, discussing The Propriety of Summary Judgment. Plaintiff did not come forward with specific facts to indicate the existence of any external cause or causes for the delay in development of facilities other than the causative factors stated in paragraph 16.

Upon the factual record submitted for the purpose of the motions, the court concluded, as a matter of law, that summary judgment was appropriate.

Plaintiff seems to suggest that it did not comprehend the purpose of summary judgment procedures. The following excerpts from an oral hearing on the motions reveal some of the court's efforts in furtherance of the very mission of such procedure—to pinpoint the issues and assess the proof to see whether there is a genuine need for trial (Dressler v. MV Sandpiper, supra, at 132):

> "[PLAINTIFF'S COUNSEL]: I think that it is quite clearly conceded, your Honor, on this No. 2 motion that the production of U.S. Steel was diminished by somewhere in the neighborhood of a million tons of finished steel products going out the door.
>
> "THE COURT: How about the cause?
>
> "[PLAINTIFF'S COUNSEL]: The cause of that is—
>
> "THE COURT: Is that in any place conceded by any of these admissions, these numbered admissions?
>
> "[PLAINTIFF'S COUNSEL]: Yes, sir. I would say that the first 110 admissions in general lead to that conclusion. It is quite clear from these that the primary reason for the finished steel production to be down is because there was a shortage of hot metal, in the neighborhood of two million tons, in each of the years 1947 and 1948." (SM, June 3, 1969, pp. 89–90)
>
> * * * * * *
>
> "THE COURT [after plaintiff's counsel had noted that two million tons of hot metal amounted to approximately ten per cent of what was contended to be normal production during 1947 and 1948]: Is that the only particular indication of what shortage of materials means, in light of 16 of the joint statement?

"[PLAINTIFF'S COUNSEL]: No. 16—

"THE COURT: You are speaking of the term 'Shortage of materials.'

"[PLAINTIFF'S COUNSEL]: In 16 that refers—

"THE COURT: 'War,' it says.

"[PLAINTIFF'S COUNSEL]: Yes. 16 relates to the entire period 1941 to 1948 and relates not to the shortage of hot metal as such but to the fact that because a war was on, and then because we were in a post-war period where the shortages continued, we were unable to maintain normal development and expansion of beneficiating facilities.

* * * * *

"16 relates to the fact that we were unable to keep that process going during the war and post-war periods, so that as we got into differing coal bodies and differing ore bodies we didn't have the beneficiating machinery to deal with those different types.

"THE COURT: Why do you say that you didn't?

"[PLAINTIFF'S COUNSEL]: We say we didn't for the reasons in 16 * * *." (SM, June, 1969, pp. 93–95)

* * * * *

"THE COURT: Of course as far as facts are concerned if a person, a party against whom a motion is made for summary judgment, doesn't submit sufficient facts, it may lead to a result against that party. I am speaking bluntly about it.

"[PLAINTIFF'S COUNSEL]: Yes, your Honor. We recognize that and we have got 120 paragraphs of facts [110 paragraphs in the joint statement plus plaintiff's statement appended to the joint statement] which we believe are clearly sufficient to bring us within [the statute]." (SM, June 3, 1969, p. 132)

The excerpts from the oral hearings contained above and in the court's opinions of July 1, 1969 are not

cited as evidence. Rather, the comments by the court, and by both plaintiff and defendant, serve to illustrate that plaintiff was, or should have been, aware of the obligations of both parties during summary judgment proceedings.

Plaintiff's reliance on Padovani v. Bruchhausen, 293 F. 2d 546 (2nd Cir. 1961), is misplaced, because that case did not involve the well-established summary judgment procedures under both the Federal Rules of Civil Procedure and the General Rules of the Southern District of New York.

IV

Plaintiff maintains that there is no distinction between the "war-induced shortages of men and materials" relied upon as an external cause of production difficulties on Motion #2, and the shortage of materials caused by the Japanese invasion of China in 1937, which was proposed as a hypothetical qualifying abnormality in the Treasury Department Bulletin on Section 722, supra at ¶5145.13. (Plaintiff's memorandum, August 8, 1969, pp. 31–32)

However, the Japanese invasion and the attendant shortage of materials from China were not occurrences affecting business in general within the United States. Nor were the occurrences directly attributable to United States government policies during World War II. If a United States taxpayer could have established that the Japanese invasion of China which caused materials shortages affected only a reasonably-limited number of other taxpayers, it is conceivable that such an invasion could have constituted a basis for relief within the meaning of either the World War II or Korean statute.

Referring to Motion #3, plaintiff suggests that the court did not consider sufficiently the item in para-

graph 45 of the joint statement to the effect that "the normal forces of competition alone were inadequate to keep the prices on steel products down." (Plaintiff's memorandum of law, September 22, 1969, pp. 3-4) However, the court weighed all the factors specifically suggested by the plaintiff that were beyond the realm of competitive pressures. As a matter of law, the court concluded in its opinion on Motion #3 that the additional factors submitted were not shown to consist of more than the valid exercise of governmental regulatory authority.

Plaintiff maintains that the Korean Act was intended to be more liberal to taxpayers than its World War II counterpart. (Plaintiff's memorandum, August 8, 1969, p. 33) Insofar as this alleged distinction refers to *quantitative* considerations, it may have some validity. Nevertheless, the relevant words of § 442(a) concerning the establishment of *qualifying* abnormalities are basically unchanged from the words of § 722(b). As Judge Friendly, speaking for the Second Circuit in Oxford Paper Co. v. Commissioner, 302 F. 2d 674, 679 (2nd Cir. 1962), observed:

> "* * * * (W)e cannot properly assume that Congress intended the same words to mean something different than before without clearer instructions than anything Congress has given here. * * *"

Upon studying the memoranda of law submitted by the parties, I conclude that plaintiff's motion for reargument should be denied.

Although my original opinions of July 1, 1969 contained the phrase, "Settle judgment on notice," I now direct the parties to prepare and submit a pretrial order which shall, among other things, provide for

elimination of the issues decided on these motions and set forth the issues remaining for trial.

The court's opinions on the motions by the parties in this case constitute interlocutory adjudications. See 6 Moore's Federal Practice § 56.20[3.—1], at 2750 (2d ed. 1966).

So ordered.

RICHARD H. LEVET,
United States District Judge.

Dated: NEW YORK, N.Y., *October 2, 1969.*

APPENDIX C

United States Court of Appeals for the Second Circuit

Docket Nos. 35655 and 35788

No. 790—September Term, 1970.

(Argued May 13, 1971 . Decided June 22, 1971)

UNITED STATES STEEL CORPORATION,
PLAINTIFF-APPELLANT

against

UNITED STATES OF AMERICA, DEFENDANT-APPELLEE

Before: FRIENDLY, *Chief Judge*, WATERMAN, *Circuit Judge*, and ZAVATT, *District Judge*.*

Appeal by a taxpayer in a refund action from a judgment of the District Court for the Southern District of New York, Richard H. Levet, *Judge*, 270 F. Supp. 253 (1967), 305 F. Supp. 497, 508, 516 (1969), 316 F. Supp. 990 (1970), granting judgment for plaintiff on one of its claims and in all other respects dismissing its complaint. Affirmed in part, reversed in part, and remanded.

*Of the District Court for the Eastern District of New York, sitting by designation.

FRIENDLY, *Chief Judge.*

In this action in the District Court for the Southern District of New York, United States Steel Corporation sought large refunds of federal income and excess profits taxes for 1950. The issue with respect to income tax involved solely a question of law concerning the respective rights of the lessor and the lessee of Minnesota iron mines to percentage depletion; it was decided adversely to U.S. Steel on the Government's motion for partial summary judgment, 270 F. Supp. 253 (1967). The other claims concerned the Korean excess profits tax for 1950; it will be as well to reserve statement of them until we have discussed the issue of percentage depletion.

I. *Percentage depletion*

The facts giving rise to this portion of the case are sufficiently stated in three paragraphs of the complaint:

> In 1950, Plaintiff was lessor and lessee of iron ore mining properties in the State of Minnesota. Pursuant to the terms of the leases, for 1950 the lessee paid Minnesota ad valorem taxes with respect to the mining properties and Minnesota royalty taxes with respect to royalties paid by the lessee.
>
> In determining the Federal income tax for 1950 which Plaintiff has paid, for purposes of §.114(b)(4) and the determination of the depletion deduction allowable under § 23(m), the Minnesota ad valorem taxes and the Minnesota royalty taxes have been included in the lessor's "gross income from the property," and have been excluded from the lessee's "gross income from the property."
>
> These adjustments were erroneous, and by reason thereof, in determining the Federal income tax for 1950 which Plaintiff has paid,

deductions for depletion have been allowed in the amount of at least $304,323.54 less than the amount which should have been allowed."

Both sides moved for partial summary judgment on this issue; the district court granted the Government's motion, 270 F. Supp. 253 (1967).

A deduction for depletion, based broadly on "the theory that the extraction of materials gradually exhausts the capital investment in the mineral deposit," 4 Mertens, Law of Federal Income Taxation § 24.02 at p. 7 (1966 rev.), has been allowed in one form or another since the Revenue Act of 1913. *Id.* §§ 24.06–24.15b. The general problem of allocating the depletion deduction between lessor and lessee was first dealt with by Congress in the Revenue Act of 1918. Section 214(a) (10) of the 1918 Act, 40 Stat. 1068, provided that "[i]n the case of leases the deductions . . . shall be equitably apportioned between the lessor and lessee." See § 234(a) (9), 40 Stat. 1078–79, for the identical provision with respect to the corporate income tax. Percentage depletion, i.e., depletion based on a stated percentage of "gross income from the property" (defined, insofar as here relevant, as "gross income from mining") rather than on the cost of the property, originated, but then only for oil and gas wells, in the Revenue Act of 1926, § 204(c) (2), 44 Stat. 16.[1] Six years later in the Revenue Act of 1932, Congress addressed itself specifically to the problem of apportioning the depletion deduction between lessor and lessee with respect to percentage depletion. In addition to retaining the "equitable apportionment" provision, § 23(l), 47 Stat. 181, Congress, in rewriting the provision for depletion of oil and gas wells with respect to a percentage of the tax-

[1] For the treatment under earlier acts, see 4 Mertens, Law of Federal Income Taxation §§ 24.04–24.11 (1966 rev.).

payer's gross income from the property and in extending this to coal, metal and sulphur mines, § 114 (b) (3) and (4), 47 Stat. 202–03, inserted the phrase:

> excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property.

The statutes here relevent, §§ 23(m) and 114(b)(4) of the 1939 Code, do not differ in any significant way.

In a case decided in 1934 with respect to the tax years 1925, 1926 and 1927, the Supreme Court held in effect that the provision of the 1932 Act for the deduction of royalties from the gross income of a lessee stated a result that would have been reached without it, since Congress could not have intended one consequence when the lessee turned over royalty oil in kind to the lessor and a different one when the lessee sold the oil and paid the lessor in cash. *Helvering* v. *Twin Bell Oil Syndicate,* 293 U.S. 312, 321 (1934).[2] The decision did not speak to the question here at issue, whether the deduction from the lessee's gross income (and the inclusion in the lessor's) should comprehend the payments of taxes which the lessee had contracted to make and would otherwise have been payable by the lessor.

The Regulations under the 1939 Code said nothing about excluding from the lessee's gross income amounts it was obligated to pay as taxes. They read,

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[2] The royalties were one-quarter of the oil extracted—to be paid in cash or in kind; during the years in question the royalties were apparently paid in cash. *But see* text, *infra.* The lessee was "authorized to pay all the taxes on said lands and improvements and to deduct the lessor's share thereof from the amount of royalties which shall fall due."

as had their predecessors going back to those under the 1932 Act:[3]

> In all cases there shall be excluded in determining the "gross income from the property" an amount equal to any rents or royalties which were paid or incurred by the taxpayer in respect of the property and are not otherwise excluded from the "gross income from the property."

The taxpayer asserts, and the Government has shown nothing to controvert this, that for many years the Commissioner made no attempt to require lessees to exclude from gross income taxes they were required to pay for the account of the lessor, and lessors did not seek to include such amounts in their depletable gross income.

In the early 1950's several lessors, doubtless stimulated by the established rule that "[t]axes paid by a tenant to or for a landlord for business property are additional rent and constitute a deductible item to the tenant and taxable income to the landlord, the amount of the tax being deductible by the latter," Reg. 45, Art. 109 (1921), approved in *United States* v. *Boston & Maine R.R.*, 279 U.S. 732 (1929), began to press for the inclusion of taxes, which lessees were required to pay on the lessors' behalf, in the lessors' gross income as "rents or royalties," thus requiring, in principle at least, a corresponding exclusion of these amounts from the lessees' depletable income—since "[a]t all events [the depletion provision] must

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[3] Reg. 111, Sec. 29.23(m)-1(f); Reg. 103, Sec. 19.23(m)-1(f); Reg. 101, Art. 23(m)-1(g); Reg. 94, Art 23(m)-1(g): Reg. 86, Art. 23(m)-1(g); Reg. 77, Art. 221(g).

be read in the light of the requirement of apportionment of a single depletion allowance." *Helvering* v. *Twin Bell Oil Syndicate, supra,* 293 U.S. at 321. The Bureau, doubtless responding to conflicting pressures, adopted a somewhat Solomonic course, providing for the apportionment of such taxes.[4] Dissatisfied with not getting the whole hog, Burt, a lessor whose lease there involved is also one of those in question in the instant case, brought the issue with respect to the Minnesota *ad valorem* and royalty taxes before the Court of Claims.[5] The court ruled unanimously in his favor, *Burt* v. *United States,* 170 F. Supp. 953 (1959). Speaking of the *ad valorem* tax, it reasoned:

> We are unable to escape the conclusion that under the terms of this particular lease the payment of the ad valorem taxes in the minerals in place was a part of the royalty compen-

[4] This was stated in Revenue Ruling 16, 1953-1 Cum. Bull. 173, 175–76, as follows:

> * * * in order to determine the amount of such taxes [ad valorem taxes] paid by the lessee for the account of the lessor it is necessary to ascertain the proportionate values of their respective interests in the property and to use such values as a basis for determining a ratio which is to be used to allocate the taxes between the parties. * * * The ratio may be determined by the Bureau, in case no agreement can be reached between the parties, or, if an agreement thereon is reached between the parties which is considered reasonable by the Bureau, such ratio will be accepted.
>
> * * * where ad valorem property taxes are imposed on mineral-bearing lands and the lessee pays the lessor's share of such taxes pursuant to the mineral lease on the land, such payments shall be treated as additional royalties which are excludable from the lessee's gross income and includible in the lessor's depletable gross income * * *. If there is insufficient gross income from production to cover the tax, such payments shall be treated as delay rental, a deductible expense of the lessee and nondepletable income to the lessor.

[5] Counsel for U.S. Steel submitted a brief as *amicus curiae.*

> sation to plaintiffs. But for the provision in the lease that the mineral taxes were to be paid by the lessee, the levy would have been an in rem tax against the land itself, of which plaintiffs were the actual owners. Undoubtedly if the lessee had not agreed to pay these taxes the plaintiffs would have asked for and been entitled to a larger royalty payment in cash or in an increased percentage or payment of some kind. It seems to us, in essence, that it was a part of the total production income which the plaintiffs received and therefore they are entitled to the statutory depletion allowance on their part of the total production income which includes the ad valorem tax on the minerals as a part of the compensation, rent, or royalty.

Although unnecessary to its decision,[6] it applied the same reasoning to the royalty tax, and added:

> Of course, taxes as such are not a part of royalty production for either the lessor or the lessee. In this particular case we are not holding that as taxes they are the subject of depletion but as part payment to the less[or] of his part of the depletion allowance, it being a part of the yardstick to measure lessor's share of the income from the production of iron ore in connection with the grant or privilege to the lessee to conduct the mining operations on the property.
>
> The same logic does not apply to the lessee's payment of the in rem taxes on the property. They are not a part of his income from the property, but are a part of the payment of the cost of securing the mining lease privilege on plaintiff's property. He may be entitled to

[6] The Government had conceded that for the purpose of the action "the taxpayer is entitled to include in his gross income from the mineral property for the purposes of computing his depletion allowance his . . . share of all royalty taxes paid by his lessee." 170 F. Supp. at 955.

> charge it off as a part of his expense or as a part of the cost of the property, but such taxes are certainly not a part of his production income. He is entitled to a depletion allowance on his income from the production of the property but this income certainly does not include the taxes which he may have paid.

Apparently concerned with the loss of revenue threatened in suits by lessors challenging the partial or total disallowance of taxes paid by lessees as depletable gross income, although recovery against the lessee would probably be barred by limitation,[7] see 26 U.S.C. §§ 1311–1315, the Government sought reconsideration of *Burt*, so far as concerned the Minnesota *ad valorem* tax, in *Handelman* v. *United States*, 357 F.2d 694 (Ct. Cl. 1966).[8] Its argument was that whether or not the *ad valorem* taxes were "rents or royalties," they were not depletable gross income to the lessor since they were payable in any event regardless of production. After extensive review of the Supreme Court decisions on depletion, none of which it found to be particularly relevant, the court unanimously adhered to *Burt* with respect to any year where there was sufficient production to cover the payment of the taxes. 357 F.2d at 703.[9]

U. S. Steel's multi-pronged attack on these precedents may be reduced to three essential thrusts: that

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[7] The Tax Court followed *Burt* in *Winifred E. Higgins*, 33 T.C. 161 (1959), with only scant discussion. The Internal Revenue Service thereupon revoked its prior rulings and announced it was prepared to litigate the question both ways until it was decided. Rev. Rul. 64–91, 1964–1 (pt. 1) Cum. Bull. 219, 220.

[8] Again, counsel for U.S. Steel submitted a brief as *amicus curiae*.

[9] Two recent decisions of the Tax Court have also sustained the Government's position here. *John W. McClean*, 54 T.C. 569 (1970); *John S. Thornton*, T.C. Mem. 1970–321, 29 CCH T.C.M. Dec. 1471 (1970).

for percentage depletion purposes only royalties "as such," determined by the agreement of the parties, should be treated as the lessor's gross income from the property; that even if the lessee's assumption of the lessor's tax obligations be deemed an additional "rent or royalty" within the meaning of the depletion provisions, under Minnesota law both the royalty and *ad valorem* taxes are *in rem* and hence may not be treated as primarily the lessor's obligation; and that in any event the *ad valorem* taxes are not dependent on production and hence payment of them by the lessee can under no circumstances be considered depletable income to the lessor excludable from the lessee's share of the depletion allowance.

With respect to the first point, we, like other courts that have considered them, have not found the multitude of cases on which U. S. Steel relies to be of much assistance. Neither *Helvering* v. *Mountain Producers Corp.*, 303 U.S. 376 (1938) nor *Helvering* v. *Twin Bell Oil Syndicate, supra,* which U. S. Steel suggests to mandate the conclusion that only royalties "as such" must be excluded from the lessee's gross income from the property, is truly apposite. *Mountain Producers* dealt not with the narrow problem whether payments of taxes should be considered as added royalties, but with a broader contention that the contractual asumption by the lessee of all the mining functions "as part of the purchase price of the oil," 303 U.S. at 380, should affect the allocation of the depletion allowance by allowing the lessor to include in its gross income from the property "the cost of production defrayed by the [lessee] under its contract." 303 U.S. at 379. When it rejected that contention and said that under the circumstances the cash payments to the lessor represented its return on the extraction of the resources, the Court was hardly meaning to lay

down a general rule that only cash payments made directly to the lessor may be considered as rents or royalties. *Twin Bell,* as indicated above, likewise did not deal with the question before us; indeed it may well be that in *Twin Bell* itself, some of the payments held excludable from the lessee's gross income had been made to the tax authorities, see fn. 2, although in diminution of rather than in addition to those labeled strictly as rents and royalties.

The issue in *Callahan Mining Corp.* v. *CIR,* 428 F. 2d 721 (2 Cir.), *cert. denied,* 400 U.S. 903 (1970), on which U.S. Steel also relies, was whether the lessor had an economic interest in the working interest supporting a depletion deduction based on gross income from the property or merely a net-profits, non-operating interest supporting a depletion deduction "only on the amounts he actually received as the ore is mined and sold." 428 F. 2d at 725. U.S. Steel quotes this language and apparently relies on the case for the proposition that the court cannot construct a gross income based on anything other than the agreement of the parties and that the lessor is entitled to a deduction for depletion "only on the amounts he actually received." What neither party mentions, however, is that the very issue here facing us—at least insofar as the "royalties as such" argument is concerned—was determined by the Tax Court consistently with the decisions in *Burt* and *Handelman,* which it cited. 51 T.C. 1005, 1021–22. While there appears to have been no dispute over the question, the fact is that the lessee's payment of the portion of the tax—there an Idaho "net profits" tax—for which the lessor was liable was held to be includible in the lessor's gross income. Finally, despite appellant's attempt to depreciate its force, *Louisiana Land and Exploration Co.* v.

Donnelly, 394 F. 2d 273 (5 Cir. 1968),[10] constitutes another precedent in favor of the Government in this case. The court there upheld the claim of an oil and gas lessor for inclusion in depletable gross income of a Louisiana severance tax which the lessee had paid.

U.S. Steel next maintains that even if payment by the lessee of the lessor's taxes may in some circumstances be considered as additional "rents or royalties," *Burt* and its progeny were wrong in treating Minnesota *ad valorem* tax as an obligation of the lessor which was discharged by the lessee, since the tax is merely *in rem* against the property, as, it asserts, is the royalty tax. *Marble* v. *Oliver Mining Co.*, 172 Minn. 263, 215 N.W. 71 (1927). While U.S. Steel appears to be correct in contending that these taxes are treated as *in rem* obligations under Minnesota law, it does not follow that the burden of paying them is not on the lessor's interest and that the assumption of its burden does not constitute additional rents or royalties within the meaning of the depletion statute. As stated by the Supreme Court of Minnesota:

> [T]he royalty tax is an imposition upon the lessor's right, title, and interest in the lands demised. . . . In the absense of [a] convenant [to pay the tax], the tax would, no doubt, have to be paid by the lessor to protect his title to the land. The intent of the lawmakers was to lay the burden of this tax upon the interest and estate of the one who granted the permission to mine.

Marble v. *Oliver Mining Co.*, *supra*, 172 Minn. at 266, 215 N.W. at 72. In *Fraser* v. *Vermillion Mining Co.*, 175 Minn. 305, 221 N.W. 13, 14, *appeal dismissed*,

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[10] Counsel for U.S. Steel also submitted an *amicus* brief in this case.

278 U.S. 572 (1928), the same court, in speaking of the royalty tax noted that "[t]he shifting of the burden of the tax from lessor to lessee is a matter of contract between the two. . . ." And in *State* v. *Rea,* 189 Minn. 456, 250 N.W. 41, 42 (1933), the Supreme Court of Minnesota was confronted with a case which was

> the only one that has come to our notice where the state has not collected its royalty tax from the recipient of the royalty, or from the lessee who may have stipulated to pay it as part consideration for the lease or permit under which exploring for or mining ore is done. . . .

We have no reason to believe that the Minnesota courts would regard the agreement of the lessee to pay *ad valorem* (as distinct from royalty) taxes of the lessor as anything other than "part consideration for the lease." In any event, we think it rather fanciful to assume that in entering a lease agreement the lessee's contractual assumption of state taxes, which is obviously of value to the lessor, does not correspondingly reduce the amount of cash payments which the lessor receives from the lessee upon the extraction of the ore. Indeed, we can do little better than recite the hypothetical put by Judge Jones, speaking for the court in *Burt,* 170 F. Supp. at 959:

> The writer is familiar with one oil lease contract covering 1,000 acres, only a small part of which was believed by the parties to be an area of production. The lease contract provided that the owner, for a three-year period of production should receive only a payment of all taxes by the lessee. After three years he was to receive the payment of all taxes or 1/8 of the proceeds of the oil produced, whichever was larger.
>
> Does anyone believe that in such a contract the lessee would be entitled to all the depletion

allowance and the lessor to none; or that in the event the 1/8 royalty exceeded the amount of taxes, the owner's part of the depletion allowance should be limited to the excess of payments above the amount of taxes?

Finally, U.S. Steel's contention that the payment of *ad valorem* taxes by the lessee cannot be depletable income to the lessor since they are not dependent solely on production was dealt with at length, and, we believe, correctly, in the *Handelman* opinion, so that it is unnecessary to repeat those considerations here.

If the question were arising for the first time, we should find the lessee's position somewhat more impressive, and the lessor's correspondingly less so, than the other courts that have considered the problem. One reason, not argued by U.S. Steel, is that when Congress wished to authorize a lessee to deduct sums other than rents properly so-called, it demonstrated its knowledge of how to say so. Section 23(a) of the 1932 Act, later § 23(a)(1)(A) of the 1939 Code and now § 162(a)(3) of the 1954 Code,[11] permitted the deduction of "rentals or *other payments required to be made as a condition to the continued use or possession,* for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity" (Emphasis supplied.) Cf. *Duffy* v. *Central R.R.*, 268 U.S. 55 (1925). If Congress had used the italicized words in § 114(b)(4)(A) of the 1939 Code, the Government would surely be entitled to prevail; since Congress used a narrower phrase and has allowed the variance to persist for forty years, arguably it desired "rents and royalties" to mean only payments specifically de-

[11] The lineage goes back to § 12(a) of the Act of 1916. 39 Stat. 767.

nominated as such. Although courts often indulge in such an approach to statutory interpretation, often for want of any better way to "find" an intent where probably there was none, there may be something rather irrational about it, especially in regard to revenue acts The depletion provisions in the 1932 Act were doubtless drafted by specialists on the subject, quite without regard to the long-standing provision in the deductions section; and the spectacle of the average Congressman, or even of the knowledgeable members of the Ways and Means and Finance Committees, scrutinizing the language with the powerful magnifying glass needed to detect the different phrasing of the two sections and appreciate its possible significance is somewhat unrealistic.[12]

Again there is something essentially grotesque in the notions that a lessor's depletable interest grows as a state increases rates under existing tax laws and im-

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[12] Indeed, as the Court warned in *Mountain Producers*, "[a]nalogies sought to be drawn from other applications of the revenue acts may be delusive and lead us far from the intent of Congress . . ." 303 U.S. at 381.

While U.S. Steel also urges upon us the "well established rule that where a law has been administered in a certain way over a long period of time, during which the law has been repeatedly re-enacted, the legislative intention is deemed to be in accord with the administrative interpretation," the "rule" has been followed with less than undeviating consistency, see 1 Davis, Administrative Law Treatise § 5.07 and cases cited therein (1958), and the truth of the matter, to use Justice Harlan's phrase, is that we are "left with a legislative history which, on the precise point at issue, is essentially negative, which shows with fair conclusiveness only that Congress was not squarely faced with the problem these cases present." *National Woodwork Mfr's Ass'n* v. *NLRB*, 386 U.S. 612, 649 (1967) (Memprandum of Harlan, *J.*). See H.R. Rep. No. 1492, 72nd Cong., 1st Sess. (1932), reprinted in 1939–1 Cum. Bull. (Part 2) 542; Seidman's Legislative History of Federal Income Tax Laws 1938–1861 464–67 (1938).

poses new ones (as Minnesota did with the royalty tax here), or that it is "equitable" that a lessee, in addition to paying these heavier taxes, should suffer a loss in the proportion of the gross income on which it can take percentage depletion. We are also somewhat impressed by U.S. Steel's argument that many mineral lands in Minnesota are owned and leased by the State, that an *ad valorem* tax is nonetheless imposed, that payment of such a tax by the lessee cannot be regarded as discharging an obligation of the lessor, and that the Government's position would thus result in a lessee of state lands being able to include a larger proportion of gross income as subject to depletion than the lessee of privately owned land.[12] Yet it may be said against such arguments that the logical underpinnings of percentage depletion are so elusive—some would use a stronger adjective—that it is idle to attempt principled reasoning about its division between lessor and lessee.

Moreover, despite these considerations we are bound to agree that there is much force in the arguments in favor of the lessor, well expressed in the extracts from the *Burt* opinion we have quoted. There would seem to be little sense in a rule that would attribute different tax consequences to a situation where the lessor accepted a lower royalty and required the lessee to pay the taxes and another where the lessor insisted on a royalty higher by his estimate of what the taxes would be. The arguments here forcefully made by U.S. Steel have been considered and rejected on more than one occasion by two courts particularly expert in tax matters and by another court of appeals having much experience with oil and gas leases, as well as by the able

[12] Perhaps, however, the state compensates for this by charging higher royalties.

district judge. While we are not bound by any of these decisions and would not hesitate to reject them if we were truly convinced they were in error, our beliefs simply do not rise to that height. *Burt* has been on the books for a dozen years, during which Congress has adopted a number of corrective tax measures but has not chosen to alter *Burt*. Under the circumstances we think it best to follow the uniform line of authority and leave correction, if that is called for, to the Supreme Court or, for the future, to the Congress.

II. *Excess Profits Tax*

The Excess Profits Tax Act of 1950, 64 Stat. 1137 (1951), sometimes referred to as the Korean Excess Profits Tax, imposed a heavy tax on "excess profits" for years ending after June 30, 1950, and beginning before January 1, 1954. Broadly speaking, it followed the general scheme of the Excess Profits Tax Act of 1940 (the World War II Excess Profits Tax) in determining excess profits by comparing net income during the war years either with the actual average net income during a "base period" consisting of the four preceding taxable years, § 435, or with a stipulated percentage rate of return on invested capital, §§ 436, 437, whichever was higher. A taxpayer using the average income method, as U.S. Steel did here, was allowed to eliminate the worst of the four years in determining its general average base period net income, § 435(d)(2); the company eliminated 1946. Under the Korean Excess Profits Tax only 83% of the average base period net income, plus and minus certain adjustments, could be used as a credit against wartime profits, § 435(a)(1); the corresponding figure under the World War II Act had been 95%, § 713.

Knowing that such a comparison might work unfairly in certain cases, Congress provided for a num-

ber of specific adjustments. But it recognized also that these might not be sufficiently comprehensive. It therefore included what has come to be known as a general relief provision, § 442(a), which reads in pertinent part:

> If a taxpayer which commenced business on or before the first day of its base period establishes that, for any taxable year, within, or beginning or ending within, its base period:
>
> (1) normal production, output or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during such taxable year of events unusual and peculiar in the experience of such taxpayer, or
>
> (2) the business of the taxpayer was depressed because of temporary economic circumstances unusual in the case of such taxpayer,
>
> the taxpayer's average base period net income, determined under this section shall be the amount computed under section (c) or (d), whichever is applicable.

In any year for which this section applied, a constructive income was to be computed for the affected months by applying the industry's yearly rate of return as determined by the Secretary of the Treasury, § 442(e).[14] If only one year was affected by an abnormality within the meaning of § 442(a) and the constructive income exceeded 110% of the actual, the constructive income was to be substituted for that year alone, § 442(c). If § 442(a) applied to two or

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[14] This simple method of determining constructive income was a significant departure from the World War II Excess Profits Tax, which required reconstruction on an individual basis of what the taxpayer's income would have been apart from the abnormalities. See *Oxford Paper Co.* v. *C. I. R.*, 302 F. 2d 674, 678 (2 Cir. 1962).

more years, constructive income (if it exceeded 110% of the actual) was to be used for all three years of the base period, § 442(d).[15]

U.S. Steel claimed that each of the three base years remaining after elimination of the worst year, 1946, came within the general relief provision of § 442(a). The grounds for this, summarily stated, were as follows:

> (1) With respect to 1947 and 1948, because its production was curtailed and its costs increased by abnormalities in the supply of raw materials due to causes hereafter described (the "materials" issue);
>
> (2) With respect to 1947 and 1948, because the price controls that had expired on November 13, 1946, and President Truman's request of July 15, 1947, that coal and steel companies forego price rises, prevented its making price increases it would otherwise have made to meet rising costs of goods and services, resulting in an abnormally narrow cost-price gap (the "cost-price" issue);
>
> (3) With respect to 1948, because its production was significantly curtailed as a result of two strikes, one from March 15 to April 22 and the other from July 5 to July 14, by the United Mine Workers which shut down coal-producing facilities (the "coal strike" issue) and an explosion at one of its Chicago works;
>
> (4) With respect to 1949, because of an interruption of production by a strike of the United Steel Workers from October 1 to November 11 (the "steel strike" issue).

Judge Levet found against the company on the first three issues and for it on the fourth. The first two issues were decided on motions by the Government

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[15] The foregoing is merely a crude summary, omitting many details of this complicated legislation not essential for decision of this case.

for summary judgment, 305 F. Supp. 497, 508 (1969); U.S. Steel has appealed with respect to the first of these and apparently also with respect to the second. *But see,* fn. 33 *infra.* The third and fourth issues were decided after trial, 316 F. Supp. 990 (1970). U.S. Steel has appealed from the decision against it on the coal strike issue, but the Government has withdrawn its appeal from the decision in the taxpayer's favor with respect to the 1949 steel workers' strike. The questions on the coal strike issue are largely of fact, on the materials and cost-price issues, at least at the present stage, of law. We shall deal initially with the issue concerning the 1948 coal strikes.

A. *1948 Coal Strikes*

The judge and the parties were in agreement with respect to the basic legal principles determining whether the 1948 coal strikes brought U.S. Steel within § 442(a)(1).[16] Strikes are listed in the Regulations' definition of "events," Regs. 130, § 40.442–2(3). On the other hand, the event must be "unusual and peculiar in the experience of the taxpayer"; "its occurrence" must not be "ordinarily encountered in the taxpayer's business operations." Regs. 130, § 40.442–2(3). Also "the interruption or diminution" of normal production by the unusual and peculiar event "must be significant and not trivial." Regs. 130, § 40.442–2(2).

The first breach in the harmony on this issue concerns the judge's ruling that, in determining whether the 1948 strikes were "unusual," the comparison should not be simply with previous coal strikes, of

[16] There is no need to consider the explosion at the company's South Works in Chicago, since U.S. Steel concedes in brief that its results, taken alone, were not significant enough to qualify the taxpayer for relief in the year 1948.

which there apparently had been none of serious consequence during the period of comparison, but rather with all sorts of work stoppages due to labor disputes. We see no basis for faulting this ruling on the facts of this case. U.S. Steel was not a seller of coal in any substantial degree; its business was the integrated production of finished iron and steel products and coal mining was simply a part of the process. It would be unreasonable to read § 442(a)(1) as entitling a taxpayer to relief because it had suffered a strike from a previously peaceful craft in one of the base years, although it had been the victim of equally or more serious strikes by other crafts in a period appropriate for comparison. The court selected the years 1941–45 as such a period. While U.S. Steel asserts that the court "simply disregarded the testimony of qualified witnesses about the taxpayer's experience in the period prior to 1942 because no 'statistics' were kept" for those years—testimony to the effect that during the 1930's strikes and other labor difficulties did not interrupt steel production in any serious way—it does not challenge Judge Levet's findings that "[t]he only relevant years prior to 1948 for which plaintiff has presented any statistical evidence regarding strike losses are 1941, 1942, 1943, 1944, and 1945" and that "plaintiff started in 1941 to record estimates of production losses due to strikes." 316 F. Supp. at 1008. Apart from any question of remoteness, given the lack of reliable data for earlier years, Judge Levet was justified in limiting his comparison to the 1941–45 period.

The court assumed the production losses from the two 1948 coal strikes were those alleged by U.S. Steel on the basis of its exhibits, finding it unnecessary, in light of its ultimate determination, to consider the Government's contention that these figures were ex-

cessive. 316 F. Supp. at 1011. These exhibits indicated the following loss figures:

	Thousands of tons	
	Ingots	Equivalent finished products
March-April Strike	402, 986	358, 135
July Strike	76, 870	55, 210
Total	479, 856	413, 345

The difficulty in making a comparison between these figures of lost production in 1948 and the results for the years in the period chosen for comparison stemmed from the lack of similar reports for the earlier years. During those years the company had generally prepared "Strike or Work Stoppage Reports," called Form B, which showed the loss for each type of production for each of its plants. The problem was two-fold. After so much time had elapsed, some of the Form B reports were missing for some of the years. Moreover, since they showed the loss of each type of product and in a number of cases a product loss of more than one type was recorded on individual or related reports, mere addition would result in pyramiding.

Faced with these problems Judge Levet engaged in what U.S. Steel properly characterizes as "a painstaking analysis." For two of the comparison years, 1943 and 1945, he arrived at firm figures of losses in net shipments (which the parties agreed was the appropriate loss indicator since "[i]n the steel-making industry production and total shipments are generally correlative," 316 F. Supp. at 1008) of steel products due to work stoppages; for the other three, 1941, 1942 and 1944, he was able to arrive only at a range. These findings were as follows:

REASONABLE APPROXIMATION OF POTENTIAL TONNAGE LOSS IN NET SHIPMENTS OF STEEL PRODUCTS DUE TO STRIKES: 1941–1945

	Minimum	Maximum
1941	13,456	270,852
1942	6,552	45,223
1943		246,389
1944	343,985	553,370
1945		828,639

Comparing these figures with those for 1948 cited above, he concluded that U.S. Steel had failed to show that the 1948 coal strikes had constituted "events unusual and peculiar in the experience of such taxpayer." [17]

Apart from the arguments that coal strikes should have been considered as something separate and apart from other work stoppages, and that the comparison should have included still earlier years, which we have already rejected, U.S. Steel does not seriously contest that this conclusion would follow if the factual findings were correct. It insists, however, that the judge did not succeed in doing what he plainly intended, namely, to eliminate the duplication or worse that would result from simply adding up the figures in the Form B Reports. It insists that the only way in which double or triple counting could be avoided would be to base the calculations on loss in ingots, the "bottleneck" in the production of finished steel, or—what amounts to the same thing—on a loss of finished products determined by applying to ingot losses an apparently recognized ratio of approximately 70%. On these bases U.S. Steel comes up with the following tables:

[17] Using the "maximum" figures the average loss per annum for the five years was 388,895 tons; using the "minimum" figures, such average loss was 287,804; using a mean of the maximum and minimum figures, such average loss was 338,349. The annual report for 1948 shows that total shipments of finished steel products were 20,655,000 tons. For the five years 1941–1945, total shipments averaged 20,128,000 tons.

Year	Ingot Loss	
	All Strikes	Coal Strikes Only
1941	18,715	
1942	9,441	
1943	48,000	
1944	118,721	
1945	478,500	
1948		579,856

Year	Loss of Equivalent Finished Product	
	All Strikes	Coal Strikes Only
1941	13,456	
1942	6,552	
1943	31,920	
1944	81,917	
1945	333,036	
1948		413,345

Mere statement of the theory behind U.S. Steel's calculations is almost sufficient to demonstrate its unsoundness, even ignoring the fact that some of the lost ingot figures are based on Form B reports for years in which they were concededly incomplete. Unlike the 1948 coal strikes, many of the work stoppages in the comparison years did not affect ingot production at all. Hence a comparison solely in terms of loss of ingots or of finished products determined on a ratio basis could not possibly be fair, since it fails to consider that losses of net shipments may result from interruptions in the production schedule at a stage subsequent to ingot production. While U.S. Steel baldly asserts that "loss of finished net product production does not, could not, and did not translate into loss of shipments unless equivalent ingot production was . . . lost," it points only to the rather general statements of two of its witnesses concerning the ability of the company to "shift" its production from one finishing plant to another in support of that proposition. Assuming that some shifting is possible, U.S. Steel has referred us to no evidence that such shifting in fact occurred during the strike periods so as

to eliminate all but reported ingot losses—let alone, with the few exceptions noted below, see fns. 19 and 20, a substantial portion of those losses which Judge Levet carefully determined.

No useful purpose would be served by our endeavoring to restate the methods whereby the judge determined production losses for 1941–45, an analysis filling some 20 printed pages of his opinion, 316 F. Supp. 1011–30.[18] Suffice it to say that we have carefully

[18] A word of explanation on the meaning of the "minimum" and "maximum" figures for certain years may be helpful. The minimum for 1941 and 1942 is the loss in net shipments, determined on the approximately 70% basis, see text *supra*, from losses in ingot production alone which were reported on the available Form B reports; the minimum for 1944 is the loss in net shipments, determined (a) on the approximately 70% basis, see text *supra*, from losses in ingot production alone which were reported on the available Form B reports and (b) on an approximately 90% basis (average yield of net shipments from total shipments), from losses in steel product production which were reported on the available Form B reports. The maximum for 1941 and 1942 is the loss in net shipments calculated as the sum of (a) the minimum for those years and (b) on an approximately 90% basis, see *supra*, the difference between the combined total production loss of iron, ingots and steel products, 300,000 tons for 1941 (as reported in the 1941 U. S. Steel Annual Report, p. 7), 53,000 tons for 1942 (as reported in the 1943 U. S. Steel Annual Report, p. 19, and in a non-contemporaneous summary estimate of lost tonnage from work stoppages) and the total reported ingot losses, which were used as the basis of the minimum. The maximum for 1944 is the loss in net shipments calculated as the sum of (a) the minimum for that year and (b) on an approximately 90% basis, see *supra*, the difference between the combined total production loss of iron, ingots and steel products, 871,000 tons (as reported in the 1944 U. S. Steel Annual Report, p. 12, a non-contemporaneous summary estimate of lost tonnage from work stoppages, and a contemporaneous summary of Form B reports) and the total ingot and steel product losses reported on the available Form B reports, which was used as the basis of

examined this and that while we recognize some validity in certain of U.S. Steel's criticisms,[19] the company has not come forward with any more accurate figures, as it had the burden of doing, and we surely are not prepared to brand the judge's careful findings as "clearly erroneous."[20]

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the minimum, less specified losses for ore, crushed slag, coke, and hot metal (or iron), shown on the available Form B reports.

[19] The more important of these are as follows:

For 1941, for which the Form B reports were incomplete, Judge Levet began with a production loss estimate of 300,000 tons in U. S. Steel's annual report, subtracted a known figure of 18,715 tons of ingot losses, applied a 71.9% "yield" to arrive at his minimum figure and, after deducting the ingot losses, applied a 91.6% "average yield net shipments of steel products from total shipments" to arrive at his maximum figure. More accurate data for later years, such as 1943 and 1945, suggest that the company's undifferentiated loss figures were inflated, and the maximum figure for 1941 is thus likely to be too high. We are also inclined to think that analysis of the substantial number of Form B reports available for 1944 in a manner similar to that used for the complete reports available for 1943 and 1945 might have reduced the maximum and minimum figures for that year.

[20] In its reply brief U.S. Steel has reproduced two Form B reports which do show possible duplication, not itself significant in amount. The possible duplication in at least one of these was not eliminated by the judge's methodology; as to the other, it is unclear from page 6 of Exhibit 7 of May 22, 1970, to which the judge refers, 316 F. Supp. at 1018, whether he meant to disregard this report entirely, since his reference is to a South Works report dated July 14, 1945, and the South Works report reproduced by U.S. Steel is dated July 13, 1945 (with respect to a work stoppage of July 5, 1945) whereas the South Works reports listed on the page noted are listed by the date of the work stoppage (June 24, 30, July 5, September 13, 28, 29). In any event, we draw an inference from these instances opposite to that desired by the company, since we are rather confident that if other such examples existed, U.S. Steel's dili-

B. *The Materials Issue*

Paragraph 11 of the complaint, relying on both subsections of § 442(a) claimed that U.S. Steel's normal production in 1947–48 was diminished by reason "of events unusual and peculiar in the experience" of the taxpayer and its business "was depressed because of temporary economic circumstances unusual" to it. Among the "temporary abnormalities" were "low quality of coking coal and iron ore, resulting in loss of production" and, also apparently, in higher costs.

Since this issue was decided against the taxpayer on a motion for summary judgment by the Government, we must consider assertions in the company's affidavits and depositions to be true, except insofar as these are invalidated by admissions or uncontradicted proof. Since we consider that the judge's findings, 305 F. Supp. at 501, drawn mainly from a joint statement under Rule 9(g) of the district court which he required, are not sufficiently generous to the taxpayer under this standard, a fuller statement of plaintiff's contentions is needed.

The problem concerned U.S. Steel's northern plants comprising 80% of its total production. Before World War II the iron ore for these plants, principally of high grade,[21] came from mines on the Mesabi Range in Minnesota. The coking coal came principally from mines in western Pennsylvania (Frick District coal),

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gent and able counsel would have brought them to our attention. The other Form B report reproduced in the reply brief does not support U.S. Steel's criticism since, while it is possible that the losses on finished products there reported were made up later in the year, there is no proof to that effect.

[21] That is to say, relatively low in sand and clay, collectively known as "gangue."

which was of high grade,[22] and to a lesser degree from southern West Virginia (Pocahontas coal) and western Kentucky (the Lynch District coal). Such washing of the Frick District coal which needed further "beneficiation" was done at a facility at plaintiff's Clairton, Pa. plant. Although it was foreseeable before World War II that the high grade Frick District coal would ultimately be exhausted, it was thought that the problem could be met for some years by diminishing the relative share furnished by such coal and blending this with lower grade coal to obtain a usable mixture—although ultimately beneficiating facilities to utilize lower grade coal would have to be installed. Similarly, although U.S. Steel foresaw before World War II that it's reserves of high grade iron in the Mesabi Range would not last forever, the war produced problems concerning sources of future iron production more quickly than could have been anticipated.

The enormous demand for steel induced by the advent of World War II made it necessary for U.S. Steel to maximize coal and iron ore mining and production regardless of the effect of such action on postwar operations.[23] For reasons about to be developed, the effect of this was to deteriorate the quality of coal and iron available for use in 1947 and 1948.

The Palmer and Colonial coal mines in the Frick District which had been the company's principal

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[22] That is to say, relatively low in sulphur and a variety of non-combustible materials collectively known as "ash."

[23] Figures in U.S. Steel's annual reports, submitted in evidence on the coal-strike issue, show that ore mining jumped from 24,225,000 tons in 1939 to 52,012,000 in 1942, and coal mining from 21,624,000 to 32,317,000 tons.

source of high grade coal were mined during World War II to such a degree that their reserves were rapidly depleted. Idle mines in the Frick District, on whose production plaintiff had counted for future mixing with lower grade coal, were brought into production, but this also did not suffice. Accordingly the company had to begin tapping reserves of low quality coal in Greene County. In 1944 it brought the Robena Mine in that county into full production. Although this turned out to have relatively high proportions of sulphur and ash, it was still possible to achieve satisfactory results by blending it with the high quality coals from the reopened mines in the Frick District and also by using the Clairton washer, although this had not been designed for coal of such poor quality. Realizing that a new washer would be required for the Greene County coal, plaintiff prepared specifications in 1944, but when the bids came in, it was found that the proposed plant (which was similar in concept to the Clairton washer) would be inadequate for the job due to insufficient reduction of the sulphur content in the coal. In an effort to develop a beneficiation process sufficiently effective to reduce the impurities in the Greene County coal to appropriate levels, U.S. Steel then conceived the plan of using a method (a heavy media process) that had been used for beneficiating iron ore but was novel in the coal industry. After preliminary tests indicated that this had promise, U.S. Steel took bids in the latter part of 1945, but war-induced shortages of men and materials delayed completion of the Robena washer until the latter part of 1948. When it came on line, the quality of the beneficiated Robena coal was greatly improved.[24] Because

[24] The quality of plaintiff's low volatile Pocahontas coal also deteriorated during the war years. This required devising a method whereby coals of different expansion characteristics

of these conditions and those described in footnote 24, plaintiff was obliged in 1947 and 1948 to purchase coal from other producers. Due to scarcity in supply, it was necessary to purchase relatively small amounts from many sources, with consequent lack of uniformity. In summary, as stated in plaintiff's brief, "the quality of coal available to charge plaintiff's coke ovens and the quality of resultant coke to charge to plaintiff's blast furnaces was the worst in history."

The iron story was much the same, although less specifically documented. During World War II plaintiff used its best grades of iron ore in order to maximize production. For the same reason it deferred its normal stripping program on the Mesabi Range. It was necessary to catch up on this thereafter. Also, by 1950 and 1951, plaintiff had added sintering and washing facilities that increased the average iron content in iron-bearing materials. Again, to quote plaintiff's brief, "[a]s a result of the conditions described above, the quality of the furnace burdens charged to plaintiff's blast furnaces in 1947 and 1948 was inferior to that experienced at any other time outside the base period."

Plaintiff avers that the combined effect of the conditions summarized was equivalent to the daily charging to its blast furnaces of a hundred 60-ton railroad cars of inert or harmful materials, more than had ever been charged before or since, with a consequent

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could be properly blended during washing. Construction of the Alpheus washer, which was designed to meet this and other problems, at Gary, W. Va., began in 1945. Due to the same conditions noted in the text, this did not come into operation until late 1948 or attain adequate capacity until late 1949. World War II also accelerated the exhaustion of high quality coal from the Lynch District, which plaintiff was unable to replace until after the base period.

loss of 2,000,000 tons in annual production of hot metal. Efforts to remedy this through the purchase of scrap were only partially successful, due, among other things, to a shortage of good quality scrap and a premium price. In consequence, finished steel production was at least 900,000 tons below normal in 1947 and 850,000 tons below normal in 1948,[25] with resulting adverse effect on earnings of at least $36,000,000 and $42,000,000.

On these facts we do not think it was proper to render summary judgment against the plaintiff, whatever the right decision may be after a full development of the circumstances at a trial.[26]

The district court's adverse ruling with respect to § 442(a)(1) seems to have rested primarily on the judge's belief that U. S. Steel had failed to show an "event" such as that section requires. The Regulations, § 40.442–2(a) (3), say:

> Unusual and peculiar events contemplated in section 442(a)(1) consist primarily of physical rather than economic events or circumstances. Such physical events include floods, fires, explosions, strikes, and other exceptional

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[25] Average production of ingots in the northern plants was as follows:

	In thousands of tons
1941–44	26,887
1947–48	24,597
1950–53	28,510

Shipments from these plants in 1947–48 averaged 17,783 thousand tons as against an average of 18,821 that would have been available for shipment during the 1941–44 period and of 19,957 for the 1950–53 period—the two latter figures representing 70% of ingot production.

[26] We note, for example, that figures from U.S. Steel's annual report for 1948, received in evidence at the later trial of the 1948 coal strike issue, show that 1948 shipments from *all* plants were the highest in history except for 1944 and that the 1947 figures had been exceeded only in 1941, 1942 and 1944.

> and uncommon circumstances hindering production, output, or operation.

Apart from the use of the word "primarily," we do not see why such effects of the greatest war in the world's history as we have described above should not be regarded as unusual and peculiar "physical" events.[27] Neither do we perceive why it should be material that the effects of World War II should take the form of a loss of access to suitable raw materials as distinguished, say, from the physical destruction of plants in the area of hostilities.[28] We can see no significant difference between the latter case, which surely should qualify under § 442(a)(1), and one where World War II deprived a manufacturer of access to a needed raw material, e.g., Malayan tin or rubber, and he had not been able to restore his imports to the accustomed scale in one of the base years.[29] Coming even closer to the instant case, if the

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[27] U.S. Steel noted in its reply brief below that "it is not claimed World War II itself is a basis for relief"—apparently to avoid the application of an alleged general "rule" that "[t]he valid exercise of governmental power does not constitute the basis for relief under either Section 442(a)(1) or (a)(2)," 305 F. Supp. at 504. Rather it rests its claim on the circumstances that confronted it during the base years, which it attempts to distinguish from "World War II itself." While we are not overly impressed by this distinction, we are even less impressed with the Government's attempted distinction of the "exceptions" to the alleged "governmental action" rule. Since the Government concedes that "these authorities can be viewed as holding that some forms of governmental action may provide a basis for relief under Section 442," we find it unnecessary to re-examine the "rule" itself.

[28] *E.g.*, if an American manufacturer had important plants in West Germany which were bombed out in 1945 and were not restored to normal production until after the beginning of the base period.

[29] Although § 442(a)(1) requires that the event occur "either immediately prior to, or during" the alleged untypical year in

Government had seized all of U. S. Steel's high grade coal and iron mines because it thought the company was not mining them as effectively as the war effort required, see 54 Stat. 885, 892 (1940), as amended by 57 Stat. 163, 164 (1943), had exhausted them, and had left U. S. Steel completely dependent on low grade or purchased coal and iron with consequent diminution of normal production through 1947 or 1948, we cannot see why the statutory test would not be met. The company should not fare worse for having behaved as a good citizen and voluntarily done what the Government might have compelled.

Alternatively, we fail to see why, on the affidavits and depositions before the district court, U. S. Steel did not qualify under § 442(a)(2). Subsection (2) covers situations rendered abnormal by factors other than interruption or disruption of normal production output or operation, e.g., a taxpayer producing usual volume at unusually high cost or selling at unusually low prices. However, the two subsections are closely related; as the Bulletin relating to the World War II Excess Profits Tax recognized, pp. 16–17, "the same basic cause might lead to a section 722 (b)(1) claim in the case of one taxpayer and a section 722(b)(2) claim in the case of another." 7A Mertens, *supra*, §42.121 at 719. It would seem enough to qualify under § 722(b)(2) (or 442(a)(2)) that a taxpayer's business was depressed because of being

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the base period, the Bulletin issued in connection with § 722 of the World War II Excess Profits Act, which used the same phrase with a variation not here material, § 722(b)(1) stated, p. 10, that "An event is deemed to occur immediately prior to the base period if under normal circumstances the effect of such event would not be fully manifested until a year in the base period and such effect is directly related to such occurrence." 7A Mertens, Law of Federal Income Taxation § 42.119 at 708 n. 80. (Zimet and Weiss rev. 1955.)

obliged to use low quality or high cost raw materials, if he had consistently followed a contrary course before the year in question and followed it again thereafter, at least when these "temporary economic circumstances" were not ones for which he was at fault—which the Government has not here asserted.

The Bulletin issued by the Treasury with respect to § 722 of the World War II Excess Profits Tax, at p. 18, quoted in 7A Mertens, *supra,* § 42.121 n. 42 at p. 726, gave as an example of a taxpayer entitled to relief because of temporary economic circumstances a brush company, normally importing its bristles from China, which was obliged to seek them elsewhere and accept inferior substitutes at higher prices because of the Japanese invasion of China in 1937. While in that case there was an "event," § 422(a)(2) does not require one. Presumably the taxpayer in the case put in the Bulletin would have fared equally well if the Chinese producers had simply decided to sell elsewhere but an alternate source of supply was in sight a few years hence.

We have had some concern whether the business of U.S. Steel could be said to have been "depressed" in 1947 or 1948. The annual reports received in evidence at the trial on the coal-strike issue show income after taxes of $127,100,000 in 1947 and $129,600,000 in 1948, which were the highest since 1929.[30] As against this, however, the Bulletin issued in connection with the World War II Act said, p. 16, that "In order for the depression of the business of a taxpayer to come under § 722(b)(2), it is not necessary that the taxpayer's earnings be reduced to any particular level, nor even that they be less than the average for the taxpayer's industry. It is necessary only that they be less

[30] After tax earnings during the World War II years were, of course, affected by the Excess Profits Tax.

than they normally would have been for the taxpayer in the absence of the temporary economic circumstances shown." 7A Mertens, *supra*, § 42.121 at 720. While the Senate Finance Committee report on the World War II Act, quoted at n. 10 on the same page, says that "As a general rule, high costs of production because of high costs of material, labor, capital, or other elements" would not qualify, this scarcely covers the case of temporary high costs unusual to a particular taxpayer and not incurred by the industry generally. Furthermore, despite U.S. Steel's relatively large profits in 1947 and 1948, a circumstance taken into account at least in part by Congress' decision to allow only 83% of base year profits, whether actual or constructive, as a credit against the Korean excess profits tax in contrast to the higher percentage permitted for World War II, there are indications summarized in the margin,[31] that *something* may have been going wrong at U.S. Steel during the base period in comparison to the rest of the industry.

The Government comes up with a number of other arguments which do not impress us. It says the taxpayer can point to no precedent where relief has been accorded in such a situation as this; the taxpayer makes the rather obvious response that the Government has cited none where it has been denied. The

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[31] The Secretary of the Treasury found that the average rate of return on assets in plaintiff's industry for the base period was 13.6%. It was stipulated that, using this factor, plaintiff's average base period net income would be $415,635,212. In contrast, its actual average base period net income was $270,660,471, approximately 65% of the industry average rate of return. Since plaintiff's assets account for a substantial share of the industry, a comparison between plaintiff's return on capital and the rest of the industry would show an even greater discrepancy. The explanation of this will be appropriate for development at a trial.

Government argues that the increase in capacity from the new beneficiating plants did not measure up to the quantitative tests for increase in capacity for production specified in § 444. Taxpayer answers that it was the inadequacy of that and other special relief provisions that led Congress to enact § 442. The Government points to § 450, wholly exempting from excess profits tax the portion of adjusted excess profits net income attributable to the mining of certain strategic minerals, the bulk of which had previously been imported. U.S. Steel answers that this extraordinary measure of relief does not negate the right to a proper credit for the producer of such old-fashioned but essential substances as coal, iron and steel.

In the final analysis, the difference between the Government and the taxpayer on this issue is in approach. The Government, in a commendable desire to protect the revenue and curtail further litigation (although one would suppose that Korean Excess Profits Tax litigation must be nearing its end), would read the general relief provisions with peculiar, almost eviscerating, narrowness. On its view an "event" must be a catastrophe affecting a particular taxpayer and perhaps a few others; "unusual" must be not merely unusual in the ordinary sense but unexpectable. As in *Oxford Paper Co.* v. *C. I. R.*, 302 F.2d 674, 678 (2 Cir. 1962), "we find no basis for the glosses" the Government "would impose upon what seems to us the straight-forward language of the statute." While the general "relief provisions are not considered to be a means of conferring general equitable relief on taxpayers, or to confer relief just because base period earnings of a taxpayer may be low or depressed," still "it is incorrect and unrealistic to say that equities play no part in the decision of such cases. Their weight is not to be ignored, even

if it cannot always be measured, and it is well within the legislative intent that they be viewed sympathetically in relation to the purposes intended to be advanced by these relief provisions." 7A Mertens, *supra*, § 42.117 at 632.[32] Whether U.S. Steel can show at a trial that World War II in fact created unusual problems that led to diminution of "normal production output or operation" in 1947 or 1948, or that its business during those years "was depressed because of temporary economic circumstances unusual" in its experience, we cannot now say. We hold only that summary judgment should not have been rendered against it.[33]

This opinion would be incomplete if we failed to pay tribute to the quality and quantity of effort devoted by Senior Judge Levet to the resolution of this difficult case or, more accurately, cases. We also express our gratitude for the helpful briefs and argument of counsel for both parties.

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[32] See also the statement by Randolph E. Paul, Esq., then General Counsel for the Treasury, before the New York Society of Certified Public Accountants, May 10, 1943, quoted in 7A Mertens, *supra*, § 42.117 at pp. 641–44.

[33] U.S. Steel has devoted scant attention in its brief to the "cost-price" issue—indeed, the Government assumed in its brief that "plaintiff is not even appealing" on this issue, a statement U.S. Steel does not deny in its reply brief. Nevertheless, U.S. Steel's opening brief does appear to request a remand for trial not only on the materials but also on the cost-price issue. In any event, while our discussion above indicates that we do not agree with all of the reasoning in Judge Levet's opinion on the cost-price issue, 305 F. Supp. at 508, we do not see how U.S. Steel's general allegations about the effects of price controls, political pressures, general public opinion, etc. would be sufficient to bring it within the statute. We think it wisely soft-pedaled this issue in favor of its more powerful and specifically documented argument with respect to raw materials.

The orders with respect to the depletion, coal strike, and cost-price issues are affirmed. The order granting summary judgment to the Government on the materials issue is reversed and the case remanded for further proceedings consistent with this opinion.[34] No costs.

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[34] Affirmance on the cost-price issue is not meant to prevent U.S. Steel from arguing its inability to raise prices if this should become relevant to the issue remanded for trial.

[NOTE: The opinion of the Court of Appeals as hereinabove reproduced as Appendix C reflects the changes made therein as per letter dated August 26, 1971, from the Clerk of the Court of Appeals, as follows:

(1) On p. 70, *supra*, in the fourth line of footnote 17, the figure "388,349" has been changed to "338,349";

(2) On p. 71, *supra*, in the third line from the bottom, a comma has been inserted after the word "possible"; and

(3) On p. 72, *supra*, in the ninth line, the word "it" has been inserted after the word "Suffice".]

APPENDIX D

United States Court of Appeals for the Second Circuit

At a Stated Term of the United Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-second day of June one thousand nine hundred and seventy-one.

Present: Hon. HENRY J. FRIENDLY, *Chief Judge;* Hon. STERRY R. WATERMAN, *Circuit Judge;* Hon. JOSEPH C. ZAVATT, *District Judge.*

UNITED STATES STEEL CORPORATION, PLAINTIFF-APPELLANT

v.

UNITED STATES OF AMERICA, DEFENDANT-APPELLANT

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed in part and reversed in part and that the action be and it hereby is remanded to said District Court for further proceedings in accordance with the opinion of this court.

A. DANIEL FUSARO,
Clerk.

A true copy:

A. DANIEL FUSARO,
Clerk.

By VINCENT A. CARLIN,
Chief Deputy Clerk.

U.S. GOVERNMENT PRINTING OFFICE: 1971